THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

MAJOR ARTICLES

DEPARTMENT ARTICLES

VOLUME XVI, NUMBER 1 FEBRUARY, 1940 PRICE $1.50 A COPY

THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

CONTENTS FEBRUARY, 1940

DEPARTMENTS

PUBLISHED QUARTERLY BY NORTHWESTERN UNIVERSITY
DURING THE MONTHS OF FEBRUARY, MAY, AUGUST, AND NOVEMBER

Publication office: 450 Ahnaip St., Menasha, Wis.
Editorial and General offices: Northwestern University, School of Commerce, 337 East Chicago Ave., Chicago, Ill.
The contents of the *Journal* are indexed in the *Industrial Arts Index*.

Entered as second-class matter, January 3, 1938, at the post-office at Menasha, Wis., under the Act of March 3, 1879. Additional entry at Chicago, Illinois. Acceptance for mailing at special rate of postage provided for in section 1103, Act of October 3, 1917, authorized October 12, 1922. Printed in the United States of America.

Subscription Rates: $5 a year; $1.50 a copy. Remittances may be made by personal checks, drafts, post-office or express money orders, payable to the Journal of Land & Public Utility Economics.

Agents of the *Journal* in Great Britain, B. F. Stevens & Brown, Ltd., 28-30 Little Russell St., British Museum, London, W. C. 1.

Advertising rates furnished on application.

THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

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Published by Northwestern University

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LAND & PUBLIC UTILITY
ECONOMICS

FEBRUARY
1940

VOLUME XVI
NUMBER 1

Appraising Urban Communities: Techniques and Objectives

By WILLIAM L. BAILEY*

REFERENCE here is to the sociological appraisal of urban communities, and to the stricter application of the methods of mathematical statistics to such appraisals. Perhaps a better term, in view of the economic connotations of "appraisal" and of the practical aspect involved in all value-judgments, would be community "diagnosis." The term "sociological" is used here in the inclusive sense of the English school, which makes it almost synonymous with "cultural" and at the same time does not make sociology just another special social science practically one with social psychology.

Real estate—and especially urban land economics—public utilities, public finance, marketing will all have a special stake in such appraisal. Many economic criteria are, of course, included in such ratings and appraisal, some being more purely economic (such as property ownership, occupation, wages, etc.) or economic aspects (such as financial) of various institutions and activities in the community. As a matter of fact, about half of the basal items employed by Edward L. Thorndike in his provocative little book, *Your City*,[1] published in 1939, are of this economic or semi-economic character, and the economic note dominates his argument and conclusions, almost as much as the sociological, even in the broader sense of that term mentioned above.

The appraisal of real properties in cities, much more than in the country, has usually been very limited in its outlook and scope, considering what would be the logical importance of their setting in the community. Perhaps the recent economic and social—not to mention political—cataclysm will have convinced appraisers that the "setting" is as important as the "jewel," for the methods of federal appraisals have taken on a more sociological character. Naturally, of course, the emphasis in business appraisals, as in ratings of bonds and the like, has been on the economic, directly or indirectly. How very little indeed of the great variations in ratings of communities is reflected in economic or financial ratings, or in governmental, administrative, and other

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[1] New York: Harcourt, Brace & Co., 1939.

classifications!

That such limitation of point of view, or specialism, is not sufficient to give sound knowledge of or proper direction and control to affairs is indicated by the cataclysm of crisis years when even the specialized indexes of conditions were satisfactory and indeed highly favorable. The key to the total situation or general living conditions, which is almost the field of sociology, whether for theoretical or practical purposes, lies quite beyond such special considerations. The economic is undoubtedly part, and a highly organic part, of the culture-whole; and this, so far as we are here concerned, is the community. Urban mortgages and other economic aspects of cities are of such vast scope and significance in the economic structure that sociological appraisal interests might well consider the possible merits of the appraisal of communities as a feature of sounder appraisal methods.

Such community appraisal should be not only theoretically but also practically sound in outlook and technique. The unique practical nature and relationships of value-judgments must not be ignored. So also sound appraisal will not only consider the local community as a whole, and not just one aspect, but also the system of communities, and the larger wholes of which it is a part.

Relationships versus Size

Thorndike[2] shows that there is not much correlation between the population-size of cities and their general life. He gives a correlation of only .06 for this factor with G, i.e., "general goodness" or general living conditions. It must be remarked, however, that for the special group of cities (with 30,000 population as the lower limit) which he uses, differences of population-size are not so marked or important as they are known to be in communities below that size, especially at the boundary line between rural and urban (say, 2,500 population) where great variations occur. The reason for the low correlation found for this characteristically American differential between cities is that the individual communities of the group chosen are of quite different *relationships*, i.e., because of location either within or without metropolitan districts, and as a result they display wide variations of goodness, quite unrelated to their population-size. The best communities in the country are, as readers of Thorndike will note, residential suburbs, which are the most differentiated parts of metropolitan districts and in which relationship is most vital.

In the more purely mathematical statistical approach to communities, as unit-wholes, such a relationship factor as conurbanism is likely to be submerged. Although only one in ten of American incorporated places is included in metropolitan complexes, nearly one-half of the population of the nation is within such areas, and a very large part of all places in the country are in some form of graded and organic relationship, as cities, towns, villages.

And this relationship greatly affects any comparison and variation ratings of them with respect to *local* characteristics. Refinements of data for rating which take into account residential,

[2] See *Your City*, *op. cit.*, which has followed and presented to the general public a series of professional papers, which have received wide notice and discussion generally and in conferences of specialists. Among them are the following: Edward L. Thorndike, "Variations among Cities in Per Capita Income," 32 *Journal of the American Statistical Association* 471–9 (Sept., 1937); Edward L. Thorndike and Ella Woodyard, "Individual Differences in American Cities: Their Nature and Causation," 43 *American Journal of Sociology* 191–224 (Sept., 1937); "Letters to the Editor," *Ibid.*, pp. 964–7; Edward L. Thorndike, "The Influence of Disparity of Incomes on Welfare," 44 *Ibid.* 25–35 (July, 1938).

transient, commuting relationships and thus recognize the cardinal conditions of cities as *centers* are therefore necessary for sound views.

Pioneer Appraisals

Such appraisal of cities is not altogether new. Over 20 years ago a little bulletin, published by Reed College and compiled by Professor William F. Ogburn, rated and appraised a selected list of cities.[3] The data which were available and comparable at that time were very much more limited than in recent years. The items for testing were selected because they were statistically available and because they tested whole areas or aspects of community life—at least as governments and organizations of special interests (semi-official) saw them. Briefly, the tests were for livelihood, health and vital conditions, home and family life, morals, and civic, educational, cultural, and social factors (generally). They comprised some 20 special items, taken with proper statistical safeguards, relating to incomes, costs of living, death rates, infant mortality, child labor, population married, church membership, public property, public improvements, parks, safety (fire losses), school property, teachers' salaries, school attendance, pupils per teacher, library circulation, literacy, and ability to speak English.

The cities chosen for rating were practically all "great cities" and displayed a difference totally in general living conditions of more than two to one. The ratings on the various items were not weighted except by inclusion of more tests for some aspects of the community life than others. The choice of items could be said to be a cultural one, for they were the ones which most widely and soundly had been reported on for control purposes by leading public and semi-public bodies. These were the chief items on which communities were wont to compare each other and represented standards of progress in community life. The running comment on the tables of this bulletin and the brief, trenchant foreword by W. T. Foster will approve themselves to the sociologist appraising communities as cultural complexes.

Since that time, the number of available items for comparison has increased by tenfold, but it is evidence of the substantial soundness of this pioneer method that inclusion of the new items does not much change conclusions. Nor are the resulting findings and principles of appraisal different from those summed up by Thorndike.

Increasingly a wide variety of practical interests and organizations have broadened their points of view and improved their techniques, taking into consideration many aspects of the community-at-large. Business and industrial surveys latterly include many civic and social matters. Realtors, for example, now increasingly realize that actual real estate prospects, activity, and prosperity are much less related to traditional empirical factors, such as size and growth of population, than they have been wont to suppose. Community advertising and market analysis will doubtless "shift gears" not a little as a result of these more logical appraisals of communities. Public relations activities of all kinds will be clarified. Publicity will see community life in a new way. Many institutions and interests in community life will see themselves in a new light. It is in this light that methods of appraisal of communities must be judged and not alone in the cold light of theoretical statistical perfection.

After all, the strictly theoretical must

[3] "A Statistical Study of American Cities," *Reed College Record*, No. 27, Dec., 1917.

recognize that it is servant to the much larger sphere of practice. One does not need to be a Pareto or a Schopenhauer to recognize the paramountcy of practice in human life and society—at least up to the present time. Jane Addams once said that "the best is the enemy of the better," and in dealing with social reality a spurious accuracy is a dangerous and not very worth-while will-o-the-wisp to follow.

In appraisals such as Thorndike's the growing penchant for strictly statistical technique in social science leads to the inclusion of statistically suitable data which have, however, little or no cultural significance.

On the other hand, the choice of items to be included out of the many hundreds of ratings on all sorts of matters which are available is significant and challenging. One might, for example, contrast it with the almost 400 items which were used as basis for scoring communities in Wisconsin in 1925.[4] Here the method is frankly empirical, the items included, their arrangement, and the scoring values assigned to each were based on the stated judgments of specialists or were the standards set out by such bodies as the American Library Association. Standards so introduced are highly significant in the appraisal process for they represent values of both theoretical and practical importance. Furthermore, such standards exist for almost every organized interest in the country, because these organizations find it necessary not only to analyze their field theoretically but also to direct and control it by definitive standards measuring values in a practical way. This is to derive value-judgments from the only legitimate field available and within which they can alone hope to be practical, once adduced and displayed.

In this connection Thorndike's report on the expressions of judgment of a certain number of educators, business people, clergymen, social workers, reformers, and the like, did not check at all closely with the statistical appraisals, although the results of the Wisconsin method and Thorndike's as well as Ogburn's are remarkably similar. It is obviously better to have the official pronouncements on values of organizations than individual judgments, since they are more cultural in significance. In fact, there seems no other way to get at cultural values.

Thorndike's Appraisal Evaluated

Thorndike's selection of items for his G, or "general goodness," i.e., general living conditions, can be called cultural choices. The 37 items chosen for this preliminary appraisal were such cultural traits as he says "all reasonable persons will regard as significant for the goodness of life for good people in a city." The list is as follows: the general death rate; infant death rate; death rate from appendicitis; per capita expenditure for schools as a whole, for teachers' salaries, for textbooks and supplies, and for libraries; average salary paid to public elementary school teachers; average salary paid to public high school teachers; percentage of persons 16–17 years old attending school; per capita expense for recreational facilities; per capita park acreages; infrequency of extreme poverty; infrequency of less extreme poverty; infrequency of work for boys 10–14 years of age and for girls of the same ages; the average wage for workers in factories; frequency of home

[4] See "How Good Is Your Town," *Bulletin*, University Extension Division, University of Wisconsin, 1925; Aubrey W. Williams, " 'Better Cities' in Wisconsin," 55 *Survey* 207–8 (Nov. 15, 1925); Aubrey W. Williams, "Wisconsin Fights It out for the Best City," 34 *American City* 61–3 (Jan., 1926).

ownership; amount of support of the local YMCA; the excess of physicians, trained nurses, and teachers over male domestic servants in the population; ownership of automobiles; installations of gas, electricity, telephones, and radios; illiteracy; the combined per capita circulation of certain popular magazines of recognized better grade; the infrequency of deaths from syphilis, homicide, and automobile accidents; the value of the city's property in schools, libraries, museums, parks, and other recreational facilities; the percentage which that is of the other property; and the value of all the city's public property (except streets and sewers) minus its debt.

This list, it will be seen, amplifies the lists given or referred to above in the pioneering studies of Ogburn and Williams. Since the items represent the personal selection of Thorndike only in the sense that they have more statistical soundness than the other 5/6 of those more or less available, it should rather be counted as "cultural," as definitive and persistent evidence of culture-traits of American cities and those most important to their fortunes and destinies. Although not entirely impeccable statistically, as professional criticism shows, perhaps this is not to be expected in culture-traits. Perhaps also Thorndike might reply that there are degrees of reasonableness in the various parts and aspects of cultures.

It seems proper to regard this list as reflecting marked and vital culture-traits of American cities since good data exist for them for some 200 or 300 cities. The sources of the data, too, included a wide variety of organized interests in our cities, ranging from governmental bodies to all sorts of theoretical and practical organizations. One may assume a critical attitude—largely personal or at least highly specialized—toward any or all of these items, and ask questions as to their nature and significance for which there is no ready scientific answer, but the very fact that they exist on such a widespread scale and have existed so persistently and expansively for many years, is a cultural phenomenon of real importance and valid for scientific notice.

However, the statistical fact that, of the total range of nearly 200 items considered by Thorndike, only about 1/5 were valid for establishing G or "general goodness," or what might be called standard general living conditions, is significant of culture-traits more or less established and of the relative degree of *community organization* attained by our cities. One result of such appraisal work will doubtless be to reduce the variability of cities and to standardize the more evidently desirable traits.

The relatively high correlations of the large proportion of the items would seem to indicate that the collectors of such data were well advised. These are significant and vital things in community life and of real theoretical and practical concern to governments and to any and all organized interests.

Moreover, a high degree of "organicity" (May the word be used?) in city life is revealed. The items are generally largely significant for each other, not only as between pairs of items but also as between groups of items and as between parts and the whole.[5]

The rationale of basic organization—the definition, scope, and relationships of the cardinal aspects, phases, and de-

[5] A recent master's thesis, "Quantitative Method for Appraisal of Cities," by William C. Resnick, Department of Sociology, Northwestern University, 1937, significantly explores the relationship of certain pairs of items. And the literature of the journals and many thesis manuscripts, under various titles, contain a vast amount of material of the same general significance.

tailed items of community life, organization, and activities—begins to be something more than logical and to have considerable statistical proof.

For, although it is difficult, if not impossible, definitely to label and segregate most of these items or factors as economic, educational, governmental, and the like, since they exhibit several faces (e.g., school property, etc.), nevertheless if such a classification is attempted, as Thorndike does (properly, it would seem), then educational items show the greatest "weight" (47.0), followed by economic-social (44.5), health (34.5), recreational (9.5), etc. A sound and salutary perspective on community life—a thing much needed, as the extreme variability on many items shows —will thus be furthered; and, if not that, at least discussion as to what may be standard parts and functions for American cities.

What might be called the personnel group of items, or what Thorndike calls the "mental or moral facts" of the city's people, is by far the most significant for appraisal in his judgment. The personnel test shows a correlation of .69 with general living conditions, or G, "general goodness." This is considerably higher than the correlation of income or socio-economic factors.

This vital personnel test consisted of the following items: number of persons graduating from public high schools per 1,000 inhabitants; the percentage of public expenditures going to public libraries; the percentage of illiteracy of the 15–24 year olds; the per capita circulation of public library books; the per capita number of telephones; the number of dentists relative to the number of lawyers; the excess of physicians, trained nurses, and teachers over male domestics; the per capita number (reversed) of deaths from syphilis; the per capita number (reversed) of deaths from homicide. Although, in general, these will be approved, there is still much ground here for discussion by sociologists, educators, municipal administrators, and even the public generally. To this, I am sure, Thorndike would by no means object. The better organization of cities is the end-all and be-all of appraisals.

The economic or income test Thorndike finds correlated at .56 with G, "general goodness," or general living conditions. And he regards the number of income tax returns, the salaries of teachers, the salaries of employees in retail stores, the wages of employees in manufacturing plants, the purchases from retail food stores, and the rentals of houses as giving substantially "the actual per capita private income for each city."

It will be of interest to economists to find that features of community life which business and industrial surveys and many chambers of commerce have long and generally stressed show extremely slight correlations with G, or "general goodness." For example, the correlation figure for population rank is only .06; for population density, .00; for recent rate of population growth, .11; and even age and sex composition of the population shows only slight correlation. Negative correlations of significance were: the gainful occupation of girls, −.63; gainful occupation of married women, −.10; percentage of negroes, −.60; number of factory workers per 1,000 of the population, −.01.

Home rentals are outstanding in every way in the correlations and may be regarded as the acid test of community appraisal. Their elaboration is noticeable in Thorndike's work. The variations in the purchasing power of the dollar were found to be small.

An interesting appraisal method, with its own significance for neighborhood, personnel, and community appraisal, is exemplified in Chapin's living room tests and their high correlation with intelligence tests, educational standing, social welfare, and the like. This is definitely a culture-value method, and evidences the organicity of community life, and further displays the linkages between personnel, income, and general living conditions at large in the community, much as Thorndike has done.

Conclusion

Statistical and sociological objections to such appraisal of communities and the various aspects of community life seem to proceed from a rather "indoor" conception of culture and society. Quarrels over the meaning of words are a large part of the objections, but after all there is enough of common language even in the statement of these items for society and community life to proceed. It is by just such reported data on life conditions and the use of relative standings and judgments on values in community life that our culture is as "good" as it is. The important thing is not what one or another individual (be he ever so scientific) may or may not think or question but what is generally accepted and acted upon by organized society. Although it cannot be said that Thorndike is unquestionably right in all he has done, nevertheless in defining the "good" he has used what he found of values and their objective evidences in the accumulations of social data on hand. It is difficult indeed to see how anyone could avoid mixing moral judgments with statistics when statistics is being applied to this sort of thing. In actual life, phenomena are mixtures. Probably completely rational proof could not be adduced for such appraisals, for doubtless the association of factors in American city life is not governed by pure reason.

If discussions of appraisal and valuation methods do nothing more than point to the necessity for social theory and practice to come to some sense of the *relative importance* of factors in the community, it will be very worth while. Our communities are unbalanced in development, with many lags, arising largely from lack of knowledge of "first things to be put first." Surveys are too often in disrepute because of absolute lack of what information is more vital than any other.

The Passing of the Public Utility Concept

By HORACE M. GRAY*

THE term "public utility concept" is used here in a broad sense to denote that body of economic, social, and legal ideas which together constitute the institutional framework within which certain designated enterprises operate. Viewed analytically, it consists of certain economic and legal assumptions, certain social objectives sought to be attained, and certain administrative and legal procedures designed to implement these abstractions and to give them functional vitality for purposes of social control. These assumptions, objectives, and procedures will be examined critically with a view toward determining whether or not they provide a satisfactory basis for public regulation in the modern economy. No attempt will be made to trace the evolution of these ideas through the literature; rather, it will be assumed that the public utility concept, in its modern American form, is a product of the late nineteenth and early twentieth centuries, and that subsequent modification has not changed materially its essential characteristics.

During the nineteenth century, in response to the dominant belief that public interest would be best promoted by grants of special privilege to private persons and to corporations, the Federal Government, by gift, or sale for nominal sums, alienated in fee simple, and without reservation of public right, the major portion of the public domain. This basic privilege was supplemented by further federal grants in the form of patents, subsidies, banking powers, and tariffs. In the twentieth century this process has continued by means of federal grants of exclusive rights to exploit particular sectors of the public domain: hydro-electric sites (Federal Water Power Act of 1920); radio, wireless, and television channels (Federal Communications Act of 1934); public highways (Motor Carrier Act of 1935); and airways (Civil Aeronautics Act of 1938).[1] The states, following the same theory, granted corporate charters of extreme laxity; municipalities granted perpetual or long-term franchises of exclusive character. In general, the recipients of these privileges were given practically a free hand in respect to organization, finance, and price policy. They followed the historic behavior pattern of all holders of special privilege and the final result was monopoly, exploitation, and political corruption. These aggressions eventually became so apparent and so onerous that a widespread demand for legislative restraint arose, in response to which the Granger Laws, Interstate Commerce Act, Sherman Law, and the first state public utility statutes were enacted. Each sought in its own way to curb certain obvious manifestations of monopoly.

Although these laws differed in many respects—differences with which the present discussion is not concerned—they had one feature in common. They all followed the delusion that private privilege can be reconciled with public interest by the alchemy of public regulation. Consequently, none of them disturbed in the slightest degree the underlying structure of special privilege; they

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[1] Although the licenses or certificates issued under these statutes purport to reserve to the public certain rights of recovery and control, past experience affords little basis for confidence in the effectiveness of such reservations.

merely reared upon it a superstructure of restraint. Monopoly capitalism, secure in its privileges, shook off the petty irritations of regulation and continued its aggressions against the public welfare. Popular opinion still adhered to the anti-monopoly, anti-corporation tradition but became increasingly confused and bewildered. Unable to detect the real source of difficulty, people were disposed to condemn existing political administrations for failure to enforce the law or to believe that additional legislation of the same character would solve the problem."[2] It was during this period of confusion, and out of this conflict between liberal ideology and the realities of monopoly capitalism, that the public utility concept evolved. When, shortly after the turn of the century, it assumed definitive modern form in the laws of Wisconsin and New York it bore the birthmarks of the political and ideological miscegenation from which it sprang.

The Concept in the Twentieth Century

The public utility concept retained and reaffirmed the basic fallacy of the late nineteenth century—namely, that private privilege can be reconciled with public interest by means of public regulation. True to the liberal tradition, it assumed a fundamental harmony between private and public interest; this being the case, specific instances of conflict were regarded as temporary aberrations or maladjustments which in no wise vitiated the general rule. The "visible hand" of public regulation was substituted for the "invisible hand" of Adam Smith, and the continuous ministration of regulation, it was assumed, would suffice to maintain a perfect balance between private and public interest. The fact that this theory had not worked with much success for the past generation in other sectors of the economy seems not to have disillusioned its advocates or to have lessened their faith that it could be made to work in the special field of local utilities.

But the public utility concept went far beyond nineteenth century theory. Whereas formerly it had been assumed that competition was generally beneficent and should, therefore, be preserved, it was now assumed that, in certain areas at least, competition was undesirable and should, therefore, be eradicated by state action. This new economic philosophy received general legislative sanction by the states between the years 1907 and 1920, and, more recently, by the federal Congress in respect to interstate operations in communication, electric power, motor transport, air transport, and natural gas. Thus, between 1907 and 1938, the policy of state-created, state-protected monopoly became firmly established over a significant portion of the economy and became the keystone of modern public utility regulation. Henceforth, the public utility status was to be the haven of refuge for all aspiring monopolists who found it too difficult, too costly, or too precarious to secure and maintain monopoly by private action alone. Their future prosperity would be assured if only they could induce government to grant them monopoly power and to protect them against interlopers, provided always, of course, that government did not exact too high a price for its favors in the form of restrictive regulation. If political manipulation should fail to remove this last source of danger, the

[2] See Thurman W. Arnold, *The Folklore of Capitalism* (New Haven: Yale Univ. Press, 1937). In Chapter IX, Mr. Arnold shows how the anti-trust laws satisfied the prevailing ideology but actually encouraged combinations. The same reasoning is applicable to other efforts at public control, including public utility regulation.

Supreme Court could be relied upon to restrain any overly zealous regulatory commission.

The obvious conflict between the traditional ideology and the public utility concept was resolved by resort to rationalization. It was said that enterprises supplying gas, electricity, street transportation, water, and telephonic communication were "inherently" or "naturally" monopolistic; that they had certain "natural characteristics" which distinguished them from other enterprises and caused them to follow different laws of economic organization; that, because of this "natural" force, they tended "inevitably" to become monopolies; that all efforts to maintain competition had failed and, by the very nature of the case, were foredoomed to fail. Thus, the fiction of "natural monopoly" was invented to explain the centripetal tendencies then observable. Government, being powerless to resist this "natural" trend, must perforce bow to the inevitable and accept "natural" monopoly as a principle of public policy. Such a conclusion did not contradict traditional thought for these new monopolies were different; they were "natural" whereas other monopolies were, by contradistinction, "unnatural" or artificial. Thus, by a soothing process of rationalization, men are able to oppose monopolies in general but to approve certain types of monopolies.[3]

But one rationalization led to others. Since these monopolies were "natural" and since nature was beneficent, it followed that they were "good" monopolies. Government, being responsible for promoting public welfare was, therefore, justified in establishing such "good" monopolies and using its power to prevent invasion by interlopers. Moreover, those who "devoted" their property to this "good" cause were entitled to have the power of the state invoked in their behalf to insure them a "fair return on a fair value." A "natural" monopoly, being a "good" monopoly, would not behave after the fashion of "bad" monopolies. Subject to an occasional propensity to indulge in excessive charges and discriminations—aberrations that would be curbed by regulation—these monopolists would organize production efficiently, utilize resources to the best advantage, employ the best techniques available, maintain high standards of service, develop their markets completely, secure capital at least cost, and in general manage their affairs to the best interests of the public to whose service they had "devoted" their property. The profit motive, although restricted, would as in competitive business, provide the incentive for efficient performance. The role of the state would be entirely negative; its interference would be confined to preventing excessive charges and discriminations.

Uses and Abuses of the Concept

It is difficult, if not impossible, to identify precisely the social objectives

[3] For a brief discussion of the contribution of economists to this rationalization see George T. Brown, *The Gas Light Company of Baltimore* (Baltimore: Johns Hopkins Press, 1936), c. VI. See also my review of this monograph in 26 *American Economic Review* 535 (Sept., 1936) in which I pointed out that Dr. Brown had failed to give proper attention to the institutional factors that underlie such monopolies. My conclusion on this point was: "Franchises, way-leaves, contracts, charters, patents, secret agreements, injunctions, dummy corporations, cut-throat competition, newspaper and banking influences, and political corruption are the institutional ingredients from which monopoly was forged by skillful and unscrupulous manipulators. A critical evaluation of these elements might have shed considerable doubt upon the 'naturalness' of this and similar monopolies." For a similar view, with respect to the so-called *inevitability* of industrial monopoly, see the statement by Leon Henderson in "Investigation of Concentration of Economic Power," *Hearings* before Temporary National Economic Committee, Pt. 5, pp. 1974–5 (Washington: Government Printing Office, 1939).

of the public utility concept during this period of confused rationalization. Certainly many of the proponents of public utility regulation intended it to protect consumers against excessive charges and discriminations; all the early state laws bear witness to this intent. It should be remembered, however, that behind this laudable social purpose lurked the sinister forces of private privilege and monopoly. They desired immunity from prosecution under the anti-trust laws, legal validation of their privileges as property rights, the protection of the state for their monopolies, and a relatively free hand to extend their economic power. All these objectives they attained under the public utility status.[4] In addition, they secured *gratis* something equally important—public acceptance and legal recognition of the economic fiction of "natural" monopoly.

Whatever relative weight may be assigned to these conflicting objectives in pre-war legislation, it seems clear that protection of consumers faded into the background during subsequent years. In the war period emphasis shifted to the problems of providing adequate service facilities, obtaining much needed capital, and adjusting rates upward to cover rising costs. After the war the utility industries entered upon a boom period during which rapid expansion was the guiding principle of both private and public policy. Private financiers and promoters were concerned with new construction, finance, consolidation, elimination of residual competition, organization of great economic empires, and speculative profits. Public regulation, in so far as the interests of consumers were concerned, practically ceased to function; the policies of commissions and courts, particularly the latter, were calculated to promote the expansionist and profit-seeking activities of private enterprise. When, after 1929, the drastic curtailment of consumer purchasing power gave rise to a widespread agitation for reduction of utility rates, commissions and courts came to the rescue of the hard pressed utilities and prevented, or minimized, rate reduction by invoking a tortured construction of the "fair return on fair value" doctrine. In extreme cases, as in railroads, rates were actually raised at a time when by every criterion of economic teaching they should have been lowered. It thus became increasingly apparent that "protection of consumers" had been superseded in large measure by "protection of property." Recently an even more menacing and anti-social use of the public utility concept has developed. In order to preserve obsolete economic organization, it is now proposed to invoke this concept to prevent the establishment of alternative institutions designed to serve needs not adequately provided for under existing arrangements. A number of examples may be cited to illustrate this latest stage of "institutional decadence."

The railroads have long sought to curb the development of motor transport by securing its inclusion within the restrictive confines of the public utility status. They have sponsored, and obtained, federal and state legislation designed to restrict competition by forcing motor carriers, as a condition precedent to operation, to apply for certificates of convenience and necessity;[5] the rail-

[4] Burton N. Behling, *Competition and Monopoly in Public Utility Industries* (Urbana: Univ. of Ill. Press, 1938). In Chapter IV, Dr. Behling shows how the policies of commissions and courts tended to strengthen and protect monopoly without at the same time curbing its aggressions.

[5] "Regulation of Motor Carriers of Persons," *House Report* No. 783, 71st Cong., 2nd Sess., 1930. In a minority report, Congressman George Huddleston described the purpose of the proposed legislation as follows: "It [the bill] was proposed and urged by the bus operators

(*Footnote 5 continued on page 12*)

roads, of course, have opposed the granting of such certificates. In Illinois, for example, the Commerce Commission, operating under a public utility statute, is reported to have granted 21 exclusive certificates on main highways.[6] This state-creation of private monopolies on the public highways aroused such protest that the legislature, after an investigation, transferred jurisdiction over motor trucks to the Department of Public Works and Buildings, and displaced the public utility type of regulation by police regulation designed to insure public safety.[7] Recently, the Association of American Railroads has disseminated a report in which it is proposed that all highways and waterways be declared public utilities and that privilege taxes or fees, sufficient to defray all costs, be levied upon those who use them.[8] This contention seems to have some judicial support, as exemplified in the Brashear case, where a lower federal court, in upholding certain taxes levied on motor carriers, said:

"The highway system owned by the state and its subdivisions is a public utility supplying facilities which constitute an actual monopoly which is subject to inter-government regulation and control. The annual cost of operating such utility should be determined in the same manner as for a privately owned utility."[9]

In the field of electric power, private companies, on numerous occasions, have invoked the public utility concept to prevent or to hinder the development of public organizations for producing and

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(*Footnote 5 continued from page 11*)
and the rail carriers, and their affiliated interests. The main purpose of its proponents is to secure themselves against competition. This is to be accomplished through the device of the 'certificate of convenience and necessity.' The proponents of the bill admitted candidly that its main purpose was to give a monopoly, to eliminate competition. The main purpose of this bill is to create a monopoly in a situation which would otherwise be highly competitive, and then to make of the monopoly an excuse for regulation. This legislation is merely a part of the general effort of an important school of business men to get away from the competitive system." (Summarized from pp. 16–9.)

Later, Joseph B. Eastman, as Federal Coordinator of Transportation, stated: "The demand for regulation of the motor-transport industry began with the railroads"; and "The railroads have spent too much time and attention on plans for the restriction of their competitors and too little on the development and improvement of their own service and the readjustment of their own rates." ("Regulation of Transportation Agencies," *Sen. Doc.* No. 152, 73rd Cong., 2nd Sess., 1934, pp. 33 and 35.) Moreover, there can be no doubt that the railroads played an important role in securing the passage of the Federal Motor Carrier Act of 1935.

[6] Statement of Senator Louis J. Menges, as reported in the *Chicago Tribune*, Dec. 14, 1938.

[7] Illinois Truck Act, Ill. Rev. Stats. 1939, p. 2162.

[8] "Highway Costs," Assn. of Amer. Railroads, Jan. 30, 1939; see especially c's I and II. The Transportation Association of America, in "A National Transportation Program," Vols. I and II and Supp. No. 1 (Chicago, 1938), urges that all forms of transport be brought under uniform regulation administered by the Interstate Commerce Commission. The National Highway Users Conference, however, in "Highway Transportation Re-Makes America" (Washington, 1939) maintains that the highways should be free. It states at p. 5: "Freedom of the highways is again being threatened in the United States—not by toll gates erected by men in the attempt to convert the public highway into a private business, but by drastic restrictions and punitive taxation whose effect is to curb the movement of persons and goods over the highways. Imposition of heavy burdens upon highway users is inspired by interests which hope to profit from the resulting curtailment of the use of highways." And again, at p. 10: "to the average person free access to the highways seems to lie in the same category as free access to the air and sunlight." On p. 20 an excerpt from the Dillman Report is quoted to the effect that *highways are not public utilities*. Whereupon the Association of American Railroads, speaking through its economist, Dr. C. S. Duncan, issued a counterblast entitled "The Answer to Highway Propaganda" (Washington, 1939) in which, after attempting to expose and discredit the National Highway Users Conference, Dr. Duncan closes with the dire foreboding that "unless highways are considered as public utilities and every user of the improved highways is charged fairly for his use of these facilities, we are headed directly for a socialized industry" (p. 20).

[9] *Brashear Freight Lines, Inc. v. Hughes*, in the Dist. Ct. of the U.S. for the So. Dist. of Ill., So. Div., In Equity DC 2273 (1938). See also Edward D. Allen, "Highway Costs and Their Allocation," 15 *Journal of Land & Public Utility Economics* 269–76 (August, 1939) and 404–15 (November, 1939). Professor Allen favors the *public utility* approach and, after outlining the theoretical justification for this view, attempts to derive a practical formula for allocating costs to highway users.

distributing electricity.[10] They have agitated unceasingly to secure inclusion within the public utility category of municipal electric systems so that the latter, despite their institutional dissimilarity, can be forced to conform to the same rules and regulations that govern private operations.[11] They have sought to block municipal competition by the plea that their franchises and certificates are exclusive.[12] They have even maintained that the Tennessee Valley Authority, an agency of the Federal Government designed to serve economic and social needs entirely outside the public utility concept, should be amenable to the public utility laws of Tennessee and Alabama.[13] They have harassed the Authority with continuous propaganda, litigation, and investigation, much of which has been based on the charge that its policies with respect to costs, rates, finance, taxes, promotional expenses, and accounting differ from those followed by private companies.[14] They have attempted to

[10] An investigation by the Federal Power Commission reveals that private companies, from 1881 to 1935, filed 278 petitions for injunctions against 195 public authorities to restrain them from constructing electric plants. Of these petitions only 90 were filed during the 50 years from 1881–1930; the remainder, or 188, were filed between 1931 and 1935. ("Restraining Orders and Injunctions Instituted against Public Electric Projects," *Sen. Doc.* No. 182, 74th Cong., 2nd Sess, 1936.)

[11] In 1935, 12 state utility commissions claimed general, and nine others partial, jurisdiction over the rates of municipal electric utilities (Federal Power Commission, *Rate Series* No. 6, 1935, pp. 2–4). For a recent judicial decision, in which a state supreme court explicitly repudiated this contention and held that municipal electric systems are not public utilities, see *Birmingham Elec. Co. v. City of Bessemer*, — Ala. —, 186 So. 569, 28 P.U.R. (N.S.) 151 (1939).

[12] *Ala. Power Co. v. Ickes*, 302 U.S. 464, 82 L. ed. —, 58 S. Ct. 300, 21 P.U.R. (N.S.) 289 (1938); *Duke Power Co. v. Greenwood County*, 302 U.S. 485, 82 L. ed. —, 58 S. Ct. 306, 21 P.U.R. (N.S.) 298 (1938).

In these two cases a former decision of the Supreme Court rose to plague it. In 1929, in *Frost v. Okla. Corp. Com.*, 278 U.S. 515, 49 S. Ct. 235, P.U.R. 1929 B 634, the Court had held that a license to operate a cotton gin, granted under a state public utility statute, was a property right within the protection of the Fourteenth Amendment and was exclusive as against a farmers' cooperative ginning company. Mr. Justice Brandeis (Holmes and Stone concurring) dissented on the ground that a farmers' cooperative was entirely different from a commercial establishment and, hence, the discriminatory classification of the Oklahoma statute in question was justifiable. Mr. Justice Stone (Holmes and Brandeis concurring) wrote a separate dissenting opinion in which he developed the doctrine of *damnum absque injuria.* When, in 1938, the Alabama and Duke companies relied on the Frost case to substantiate their claim that municipal competition threatened to destroy their property and, hence, contravened the Fourteenth Amendment, Mr. Justice Sutherland, speaking for a unanimous Court, held that the Frost doctrine was inapplicable and that, since the competition complained of was legal, the rule of *damnum absque injuria* applied. Again, in 1939, in *Tenn. Elec. Power Co. v. TVA*, — U.S. —, 83 L. ed. —, 59 S. Ct. 366, 27 P.U.R. (N.S.) 1, the private company relied in part on the Frost doctrine. But, once again, Mr. Justice Roberts speaking for the majority, the Court held that the Frost case was inapplicable and reaffirmed the doctrine of *damnum absque injuria.* Mr. Justice Butler, however, speaking for himself and Mr. Justice McReynolds, dissented on the ground that the Frost case was applicable, and that the competition complained of was illegal and, hence, unconstitutional. It would seem, therefore, that the Frost doctrine, although never expressly repudiated, has been abandoned, for the time being at least, in favor of the rule of *damnum absque injuria.* For a criticism of this latter doctrine, and an exposition of the private utility point of view, see William M. Wherry, "Federal Competition May Be Unconstitutional—but?" 24 *Public Utilities Fortnightly* 3–12 (July 6, 1939) and 24 *Ibid.* 84–91 (July 20, 1939).

[13] *Tenn. Elec. Power Co. v. TVA*, *supra* n. 12.

[14] These charges culminated in an investigation by a Joint Congressional Committee, pursuant to Pub. Res. 83, 75th Cong. The majority report recognizes clearly the inherent differences between TVA and private utilities. The three minority members, however, refuse to concede such distinctions and insist that TVA should be subject to regulation in the same manner as private companies. In their own words: "It should be under the regulation of local State utility commissions and the Federal Power Commission in substantially the same manner as private utilities are under such regulation. . . . The TVA should be required to fix reasonable rates that would cover all costs, including operating expenses, interest on the investment, taxes, and depreciation or amortization. It should pay all Federal, State, and local taxes in the same way as taxes on similar private property *is* [as printed] computed. We recommend that the TVA define its area of distribution so that present uncertainty may be removed and the private utilities in adjoining areas feel justified in making much-needed investments for improvements and expansions." (*Report*, p. 277.)

(*Footnote 14 continued on page 14*)

block the organization of rural electric cooperatives by contending before commissions and courts that the latter should be classified as public utilities and forced to obtain certificates of convenience and necessity—which grant the private companies are, of course, prepared to oppose. Although this attempted perversion of the public utility concept ultimately failed in most jurisdictions, it has resulted in protracted delays and considerable expense to the rural cooperatives.[15] Though generally defeated in this major attack, the private power companies are still able, under existing laws, to continue their program of harassment by securing from some commissions permits for extensions that cut through territory blocked out for unitary development by cooperatives.[16]

The same tendency to invoke the public utility concept in order to forestall the development of new institutions that threaten the security of existing organizations may be observed in other fields. The radio industry, desirous of monopolizing the air but fearful that its temporary licenses may be revoked or that public broadcasting may be established, may ultimately seek refuge in the public utility concept.[17] The real estate interests of Chicago, in an effort to frustrate public housing, recently conducted an active but unsuccessful campaign for the creation of "public service housing corporations."[18] The milk monopolists, unable to suppress competition completely, unable to appease the exploited farmers and consumers, threatened in some areas with municipal and cooperative distribution and under indictment or investigation for restraint of trade, may soon find it expedient to seek admission to the public utility status, provided, of course, that the conditions imposed by government are not too onerous.[19]

(*Footnote 14 continued from page 13*)

On April 5, 1939, Rep. Rankin of Mississippi charged in the House that the minority report had been "ghost written" by private utility propagandists. Rep. Jenkins of Ohio, a minority member of the Committee, denied this. (See *Congressional Record.*) Drew and Pearson, in their syndicated column, "Washington Merry-Go-Round," of April 5, 1939, made the same charge.

[15] *Re West Tenn. Power & Light Co.*, 18 P.U.R. (N.S.) 369 (1937); *Ala. Power Co. v. Cullman County Elec. Membership Corp.*, 19 P.U.R. (N.S.) 464, 234 Ala. 396, 174 So. 866 (1937); *Carolina Power & Light Co. v. Johnston County Elec. Membership Corp.*, 20 P.U.R. (N.S.) 208, 211 N.C. 717, 192 S.E. 105 (1937); *Southwestern States Tel. Co. v. Okla. Inter-County Elec. Coop.*, 27 P.U.R. (N.S.) 321 (1938).

The West Virginia Commission is one of the few that have insisted that rural electric cooperatives are public utilities and must show cause in order to obtain a certificate of public convenience and necessity (*Re Harrison Rural Electrification Assn., Inc.*, 24 P.U.R. (N.S.) 7 (1938)).

[16] For a vigorous discussion of the obstructionistic tactics of private power companies against rural cooperatives see *Annual Report*, Rural Electrification Admin., 1938, pp. 5–6, 76–83, and 94–105. For a special form of obstruction—namely, refusal to grant satisfactory wholesale rates to rural cooperatives—see W. Clarence Adams, "Electric Cooperatives Scan Wholesale Power Rates," 22 *Public Utilities Fortnightly* 368–77 (Sept. 15, 1938).

[17] Frank Waldrop and Joseph Borkin, *Television—A Struggle for Power* (New York: William Morrow & Co., 1938), c. 22.

[18] Illinois Sen. Bill 264, introduced March 29, 1939; see *Chicago Tribune*, March 30, 1939. These corporations were to be given a broad power of eminent domain, a relatively free hand in building construction and operation, and their rentals were to be fixed in accordance with the public utility formula. It was charged by the opposition, and never successfully refuted, that the real purpose was to block out large slum areas in Chicago so that land could not be secured for public housing. Compare with the strict provisions of the existing Illinois statute governing private *housing corporations*, approved July 12, 1933 (Ill. Rev. Stats. 1939, p. 922). For propaganda in favor of these "public service housing corporations," see *Chicago Tribune*, beginning Dec. 14, 1938 and continuing through June, 1939.

[19] In 1935 I considered this question on its merits and reached the conclusion that the distribution of milk should not be a public utility. (Horace M. Gray, "Should the Distribution of Milk be a Public Utility?" *Dairy Manufacturers Conference Manual* (Urbana, Univ. of Ill., Jan. 21–25, 1935).) This judgment is not in agreement with the more favorable view expressed a year later by Professor W. P. Mortenson in "Distribution of Milk under Public Utility Regulation," 27 *American Economic Review* 22–40 (March, 1936). At pp. 39–40, Professor Mortenson says that distribution of milk as a public utility can succeed if all the interested parties

(*Footnote 19 continued on page 15*)

The air transport companies have been brought within the public utility category to the extent that they are now being given exclusive certificates of convenience and necessity.[20] The radio broadcasting interests, having built up nation-wide systems under a six months' licensing arrangement, are dissatisfied with their insecurity of tenure and are demanding indeterminate certificates of exclusive character.[21] The chronically chaotic bituminous coal industry has sought and obtained a measure of governmental protection under the Guffey Act; although this form of control does not coincide with public utility regulation, it goes far in the same direction. Likewise, the restriction and proration schemes now in vogue in the oil industry resemble public utility regulation in some respects, although they do not involve fixation of profit margins or prices by government. From the same point of view, the whole NRA experiment may be regarded as an effort by big business to secure legal sanction for its monopolistic practices and to invoke the power of the Federal Government to assist in suppressing competition. Even certain farm groups, finding themselves in desperate economic straits and observing how the mantle of governmental protection has been thrown around public utility monopolists, proclaim that agriculture should be a public utility and should receive the same protection.[22]

Enough perhaps has been said to demonstrate the "institutional decadence" of the public utility concept. It originated as a system of social restraint designed primarily, or at least ostensibly, to protect consumers from the aggressions of monopolists; it has ended as a device to protect the property, i.e., the capitalized expectancy, of these monopolists from the just demands of society, and to obstruct the development of socially superior institutions. This perversion of the public utility concept from its original purpose was perhaps inevitable under capitalism. Here, as in other areas of our economic and social life, the compelling sanctions of private property and private profit, working within a framework of special privilege, determined the direction and outlook of public policy. Just as in the days of the Empire all roads led to Rome so in a capitalistic society all forms of social control lead utlimately to state protection of the dominant interest, i.e., property. The public utility concept has thus merely gone the way of all flesh.[23]

(*Footnote 19 continued from page 14*)

cooperate to make it succeed. This last condition, however, begs the question, for experience shows that this is the very thing they will not do. After a reexamination of this question in the light of recent experience with public utility control, I am more than ever convinced that it would be a mistake to apply the public utility concept to the distribution of milk.

[20] Oswald Ryan, "The Civil Aeronautics Act of 1938," 23 *Public Utilities Fortnightly* 515–25 (April 27, 1939).

[21] *Chicago Tribune*, April 30, 1939.

[22] A federal bill of this character, the so-called "cost of production" plan, is reported to have been approved by the Senate Committee on Agriculture (*Chicago Tribune*, March 31, 1939).

[23] Professor Henry C. Simons in "The Requisites of Free Competition," 26 *American Economic Review* 68–76 (March, 1936) at p. 74 holds that: "Unregulated, extra-legal monopolies are tolerable evils; but private monopolies with the blessing of regulation and the support of law are malignant cancers in the system." He goes on to affirm that such regulation leads inevitably to fascism; he advocates the stamping out of private monopoly and the public ownership of railroads and utilities. A similar view is expressed by Professor Clifford T. James in "Commons on Institutional Economics," 27 *American Economic Review* 61–75 (1937).

The Federal Trade Commission has recently deemed it necessary to warn against the application of this doctrine to the steel business: "The classification of industries as necessary [natural] monopolies should be, in the Commission's opinion, kept to as narrow limits as technical considerations permit .... The Commission therefore suggests that the steel industry, which it believes to be capable of reasonably efficient operation without monopoly, should be definitely separated in public policy from the 'natural' monopolies, and treated

(*Footnote 23 continued on page 16*)

Obsolescence of the Concept

But aside from its perversion to anti-social ends, the public utility concept is obsolete from another point of view. As previously noted, it was designed to attain limited objectives by negative means. One may read the early public utility statutes in vain to discover any express mandate for the positive promotion of public welfare; the whole tenor of these laws is negative and restrictive; they prohibit certain obvious forms of monopolistic misbehavior but fail to impose definite responsibility for socially desirable action. Thus, public utility companies are under no legal compulsion to conserve natural resources, to utilize capital efficiently, to employ the best known techniques and forms of organization, to treat labor fairly, to extend service to non-profitable areas, to improve public health, to strengthen national defense, to promote technical research, to provide service to indigent persons, to institute rate and service policies that will foster cultural and social values, or to develop related benefits such as navigation, flood control, and irrigation. This being the case, private utility monopolosits will have regard for these broad social objectives only when by so doing they can increase or maintain their own profit. Experience has shown that they will not voluntarily strive to attain these ends; moreover, it is clear that public utility regulation, as at present constituted, cannot compel them, against their own interest, to do so. Thus, the public utility concept is functionally impotent in the sense that it is incapable of securing the social objectives that are essential in the modern economy. When any institution reaches this advanced state of obsolescence, it tends to be superseded by some new institution that is more positive in character and better adapted to the needs of the time; such a process of gradual supersession seems now to be under way.

Within recent years the "institutional inventiveness" of political leaders and public administrators has produced a number of such new institutional arrangements. Among these are: direct action by departments or bureaus of the Federal Government to supply needed facilities; public corporations chartered under both federal and state authority; multiple-purpose, regional, water-control projects; rural electric cooperatives; federal grants-in-aid; federal-state-municipal cooperation; Public Works loans-and-grants; Reconstruction Finance Corporation loans; and federal subsidy for desirable services. None of these comes within the traditional public utility concept; they all involve direct, positive action rather than mere negative restraint; they are relatively immune from restrictive, judicial interpretation of the property and due process clauses of the Fifth and Fourteenth Amendments; instead of relying exclusively on the police power of the states and the commerce power of the Federal Constitution, both hitherto narrowly circumscribed by the Supreme Court, they call into play other more positive and less restricted powers

(*Footnote 23 continued from page 15*)

as a free enterprise." ("Investigation of Concentration of Economic Power," *op. cit.*, Pt. 5, p. 2199.)

An English critic describes the fictional character of the public utility concept as follows: "In these cases (natural monopolies) it seemed best to countenance unrighteousness but to limit the plunder. A pompous and question-begging name—'business affected with a public interest'—was therefore invented by the lawyers to cover such enterprises, and they were placed under special government regulation.

"But the classification soon became a veritable Pandora's box . . . the qualifications necessary for admission to the box have changed so constantly that its present contents form a very ill-assorted miscellany, . . . and the nature of additions thereto is quite unpredictable." (A. S. J. Baster, *The Twilight of American Capitalism* (Westminster: P. S. King & Son, Ltd., 1937), p. 27.)

of the Federal Government, such as the proprietary, finance, public welfare, and national defense powers. In every respect, therefore, these new institutional devices appear more capable of serving modern social needs than do private monopolies operating under public utility regulation.[24]

Another related movement that points in the same general direction is the rise of creative economic planning by government. Under the prevailing system of monopoly capitalism, private enterprise seems to have lost, in large measure, its power to plan constructively for progressive improvement of the economy. This failure is observable in many areas and, in the utility field, is most apparent in connection with water resources, electric power, natural gas, communication, and transportation. Now this is a fatal weakness, for when private enterprise falters in the performance of this all-important creative function, government must assume this responsibility, ideologies to the contrary notwithstanding. No one who has studied this phase of the problem carefully can fail to be aware of the serious shortcomings of private enterprise in these areas, or of the significant progress made within recent years by governmental planning. No one today believes seriously that the scientific control and utilization of water resources, the perfection of socially adequate national systems of electric power and electric communications, the conservation of natural gas, and the rationalization of our chaotic transportation system can be accomplished by private enterprise operating within the framework of the traditional public utility concept. It is generally recognized that the solution of these problems will require governmental action of a quite different order than that involved in public utility regulation. This action must be positive and creative, it must call into play powers of government not heretofore brought to bear, it must rest upon a solid basis of economic and social planning, and it must be free from the creeping paralysis of judicial interference.

Even the Supreme Court, the legal progenitor of the public utility concept, appears to entertain some doubt concerning its own handiwork. In a long series of cases, from *Wolff Packing Co.* v. *Kansas Industrial Commission* in 1922[25] to *New State Ice Co.* v. *Liebmann* in 1932,[26] the Court used the public utility concept as a closed legal category with which to invalidate efforts of the states to regulate certain types of business. This narrow, legalistic interpretation evoked a rising tide of criticism, both within and outside the Court, which reached a peak in the classic dissenting opinion of Mr. Justice Brandeis in the Ice case. Finally, in *Nebbia* v. *New York* (1934),[27] Mr. Justice Roberts, for the majority practically abandoned the traditional position. Admitting explicitly that the milk business was not, and never had been, considered a public utility, he held, nevertheless, that the state of New York, if the legislature saw fit to do so, could fix the price of milk without contravening the Fourteenth Amendment. In short, the question whether or not the milk business was a public utility, or of such nature that it could properly be so classified, was irrelevant to the

[24] Horace M. Gray, "Recent Changes in the Public Control of Electric Rates," 17 *Journal of Business* (University of Iowa) 7–10 (March, 1937). In this article I analyzed briefly the contributions of certain new institutions to public control of electric rates and came to the conclusion that they are far more effective in this respect than traditional methods under the public utility doctrine.

[25] 262 U.S. 522.

[26] 285 U.S. 262.

[27] 291 U.S. 502, 78 L. ed. —, 54 S. Ct. 505, 2 P.U.R. (N.S.) 337.

main issue. The power to regulate was inherent in the state and could be exercised, both with respect to prices and other matters, if the legislature felt that conditions warranted. A minority of the Court, however, could not stomach such legal heresy. Mr. Justice McReynolds (Van Devanter, Sutherland and Butler concurring) wrote a dissenting opinion in which he restated and reaffirmed the traditional doctrine that prices could be regulated only when it was clearly shown that the business in question was a public utility or of such nature that it could be so regarded. The abandonment of this principle would, he asserted, open the door to almost unlimited public regulation of prices. This prophecy was of course correct but, as Mr. Justice Roberts pointed out, quite irrelevant.

Certain other established features of the public utility concept have likewise been attacked by individual members of the Court. In *McCart* v. *Indianapolis Water Company* (1938),[28] Mr. Justice Black, in a caustic dissenting opinion, condemned the theory of "reproduction value" as productive of interminable delays and hopeless confusion. After commenting upon the necessity for judicial prophecy to decide valuation cases, he asked: "Can a judge be found who can accurately devine all future prices of commodities to be used for imaginary reproductions of this company's property?" (P.U.R., p. 471.) He then goes on to describe the chaotic procedure of valuation:

"it is exceedingly difficult to discern the truth through the maze of formulas and the jungle of metaphysical concepts sometimes conceived, and often fostered, by the ingenuity of those who seek inflated valuations to support excessive rates. . . . Completely lost in the confusion of language—too frequently invented for the purpose of confusing—Commissions and courts passing upon rates for public utilities are driven to listen to conjectures, speculations, estimates, and guesses, all under the name of 'reproduction costs'." (P.U.R., p. 472.)

To illustrate the preposterous claims made in the name of "reproduction value," Mr. Justice Black describes, in a delightfully ironic passage, the trials and tribulations of imaginary sailors attempting to navigate the White River and the "devoted" efforts of the company to facilitate their nautical venture, thereby creating a "value" upon which the users of water in Indianapolis are expected to pay a "fair return."

Mr. Justice Frankfurter (Black concurring), in a recent dissenting opinion,[29] not only declares the *Smyth* v. *Ames* formula for valuation "moribund" but shows how the states by various devices have sought to escape it. He is prepared to approve the constitutionality of the new device involved in this particular case—namely, the temporary rate reduction order with future recoupment if necessary. In his own words:

"the court's opinion appears to give new vitality needlessly to the mischievous formula for fixing utility rates in Smyth v. Ames. The force of reason, confirmed by events, has gradually been rendering that formula moribund by revealing it to be useless as a guide for adjudication. . . . At least one important state has for decades gone on its way unmindful of Smyth v. Ames, and other states have by various proposals sought to escape the fog into which speculations based on Smyth v. Ames have enveloped the practical task of administering systems of utility regulation. . . . The statute under which the present case arose represents an effort to escape Smyth v. Ames at least as to temporary rates. It is the result of a conscientious and informed endeavor to meet difficulties engendered by legal doctrines which have been widely

[28] 302 U.S. 419, 82 L. ed. 336, 58 S. Ct. 324, 21 P.U.R. (N.S.) 465.

[29] *Driscoll v. Edison Light & Power Co.*, — U.S. —, 83 L. ed. —, 59 S. Ct. 715, 28 P.U.R. (N.S.) 65 (1939).

rejected by the great weight of economic opinion, by authoritative legislative investigations, by utility Commissions throughout the country, and by impressive judicial dissents." (P.U.R., pp. 76–7.)

The valuation doctrine has enjoyed a remarkable vitality but it is difficult to see how it can long withstand such criticism from within the Court itself. In the meantime the states, as Mr. Justice Frankfurter points out, are exercising their ingenuity to find practicable avenues of escape.

Conclusion

The conclusion is inescapable that the public utility concept, as we have known it, lacks survival value in the modern economy;[30] its limited objectives, its inherent contradictions, its negative character, and its perversion to anti-social purposes render it impotent for the solution of present-day problems. Like other outmoded institutions, it seems destined to decline in relative significance and ultimately to be superseded by new and socially superior institutions. But the "passing of the public utility concept" is not likely to proceed rapidly. It is deeply rooted in our law and social traditions; powerful economic organizations have a vested interest in its preservation as a protective device; and, as a people, our capacity for "institutional inventiveness" is poorly developed. Hence, the rate of change will probably be determined by our ability to originate and perfect new institutions that are better adapted to modern needs.

The fact, however, that the public utility concept is tending to be superseded should serve as a warning to those who propose to extend its application. Why should an obsolete institution, one that is a demonstrated failure, be extended to embrace additional economic activities? What reason is there to suppose that a system of public control which has proved ineffective in the case of transportation, power, and communications will prove successful in the case of oil, coal, milk, housing, and other forms of enterprise? Why, at the very time when it is being superseded in those areas where it has been operative for many years, should it be extended to new fields where the problems are quite

[30] Commissioner Jerome Frank, of the Securities and Exchange Commission, reaches the same conclusion in "Investigation of Concentration of Economic Power," *op. cit.*, Pt. 5. He suggests at p. 1954 that the traditional kind of "public utility regulation" ought to be severely modified, if not abandoned, and that certainly it ought not to be applied to other industries. He says (pp. 1955–6): "It doesn't seem to me that in facing new and serious problems we need to rely solely upon mechanisms and contrivances heretofore invented, regardless of their proved partial inadequacy . . . . I don't think we are obliged to fall back upon the analyses made yesterday that the only conceivable way of acting is by Government encroachment upon the activities of industry in the particular form we have used heretofore. . . . We oughtn't, so to speak, to operate on the body politic with rusty or antiquated surgical instruments. . . . I think it would help our thinking on the subject of the possible extension of the category of such industries if we could drop the use of the words 'public utility,' for, unfortunately, that phrase has now associated with it a certain kind of so-called 'regulation.' It might help our thinking if we could invent some new word—I don't know what the word would be; for lack of a better one we might call it 'ugwug'—something that has no emotional connotations, no past history attached to it and therefore doesn't call to mind all the apparatus of our present and, I think, largely inadequate method of dealing with those industries which are now in that category."

Again, p. 1959, he insists that we "must use new devices"; that (p. 1960) "we have done too little experimenting; we have closed our minds by fixed categories of what we call regulation' "; and (p. 1975) "no blanket formula [of regulation] should be applied to all."

David Cushman Coyle, in "Social Control of Production," 206 *Annals of the American Academy* 121–5 (Nov., 1939), advocates a general extension of the public utility category to include a wide range of necessary monopolies but he goes on to say (p. 125) that they should be "socially controlled, excluded from capitalist motivations, detached from all concern with book profits, and ultimately destined for public ownership." It is obvious that Mr. Coyle envisages a type of regulation quite different from traditional public utility regulation, which does not exclude *capitalist motivations and concern with book profits*, or necessarily lead to public ownership.

different and the complications more numerous? If additional sectors of our economy need to be brought within the orbit of public control, would it not be more realistic to fashion new institutions for this purpose rather than to rely on a model that has outlived its usefulness?

The view that the public utility concept is tending toward obsolescence and supersession should not, as one critic feels,[31] be construed as pessimistic or as indicating the inevitability of public ownership. All institutions are subject to the same evolutionary process in a dynamic society. They arise in response to definite social needs, serve for a time the purposes for which they were created, eventually become impotent or actually detrimental, and are gradually displaced by new institutions designed to meet new needs. The observation and analysis of this process in the economic field are proper functions of the economist and should be the objects of scientific inquiry devoid of emotional predilections. One may experience a certain nostalgia for familiar institutions and apprehension concerning new ones, but this is an emotional reaction, not a scientific judgment. The passing of an obsolete institution, although it may be noted with regret, is on the whole a proper basis for optimism, because it clears the way for the development of new institutions that are better adapted to contemporary needs. The exact nature of these new institutions is neither predictable nor inevitable. Their form will be determined by the interplay of numerous forces, many of which cannot be clearly foreseen or evaluated. Hence, in the present instance, there is no reason to suppose that the public utility concept will be displaced exclusively by public ownership. If the spirit of "institutional inventiveness" is given a free rein, many new types of control, not heretofore contemplated, may be developed. These may differ both from public utility regulation and from present forms of public ownership. The latter is merely one of several possible alternatives and is by no means inevitable.

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[31] When this paper was presented in rough outline form at the Mid West Economics Association meeting in Des Moines, Iowa, April, 1939, Professor Sidney Miller of the University of Iowa felt that its implications were unduly pessimistic and that it pointed to public ownership as the only available alternative.

The Graduated Farm Land Transfer Stamp Tax

By J. A. BAKER*

DO THE people of this Nation wish to prevent the disastrous effect of speculative booms in land values upon the conservation of the Nation's soil and upon the security and living standard of farm families?[1] If they do, the necessary device to effect this result is available through a simple amendment of existing federal legislation. The Revenue Act of 1926, as amended and extended in 1928, 1932, 1934, 1935 and 1939, provides for a stamp tax on conveyances which, if properly revised, would form an effective check on speculative activity in the land market.

Observation of the results of booms in land values has created and maintained a kind of unconscious consciousness that something should be done in a public way to discourage the speculative buying and selling of farm land.[2] All of us are familiar with the complex problems of the economic aftermath of the World War of 1914–18. In fact, governmental agencies in the field of agriculture have been struggling for more than 20 years with these problems. The debris has not even yet been cleared. Moreover, we have been so busy formulating techniques for the clean-up job that we have failed as a Nation to provide appropriate devices for preventing future recurrence of the excesses of the past. The outbreak of another European War, however, calls us abruptly from our "clean-up" tasks to a conscious knowledge of the need for constructive preventive measures. Although a great deal has been done to bring order from the chaos of agricultural depression, even these advances are endangered by the outlook for a headlong overexpansion in view of anticipated increases in agricultural exports.

We have been agreed all along, that is, most of us have been agreed, that the value and the selling price of farm land should be stabilized at a fair level determined by long-time earning capacity. The speculative land purchases in the "breadbasket of America" that have already started as a result of the present European War, moreover, indicate that a widespread knowledge of the results of past speculative booms in land values is a poor brake on the development of the same kind of psychological atmosphere that led to previous booms. If this observation is correct, it means that the envisioned goal of truly productive land values squeezed dry of all the "water" of speculative psychology can be attained only if reliance is placed on more direct and more forceful means than greater publicity and information. If speculative buying and selling of farm land are to be effectively discouraged, appropriate regulatory measures must be established.

The Stamp Tax on Conveyances

The Nation is fortunate in having at this time the fundamental outlines of the required regulatory device already established in its tax legislation. The stamp tax on deeds of conveyance was enacted by the Revenue Act of 1932 as

* Rural Rehabilitation Division, Farm Security Administration.

[1] The points of view expressed in this article are the personal opinions and observations of the author. They do not reflect the official policies of Farm Security Administration nor those of the U. S. Department of Agriculture.

[2] Attention is called to the excellent presentation, in general terms, of the historical and economic aspects of land speculation by Dr. L. C. Gray in *Encyclopedia of the Social Sciences.*

a revision to Title VIII of the Revenue Act of 1926. This amendment as enacted in 1932 is:

"Section 725, Schedule A of Title VIII of the Revenue Act of 1926 is amended by adding at the end thereof a new subdivision to read as follows:

"8. Conveyances: Deed, instrument, or writing, delivered on or after the 15th day after the date of the enactment of the Revenue Act of 1932 and before July 1, 1934 (unless deposited in escrow before April 1, 1932), whereby any lands, tenements, or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction, when the consideration or value of the interest or property conveyed, exclusive of the value of any lien or encumbrance remaining thereon at the time of sale, exceeds $100 and does not exceed $500, 50 cents; and for each additional $500 or fractional part thereof, 50 cents. This subdivision shall not apply to any instrument or writing given to secure a debt."

By the enactment of this tax on conveyances, the Congress has recognized a public interest in land transfers, and has established the principle of land transfer taxation. This means that, if some type of land transfer taxation can be used to prevent speculative activity in the land market, this device could be enacted as a simple amendment of existing tax legislation. Although the existing tax is purely a measure to raise revenue, it appears fairly certain that an appropriate amendment would give the tax a regulatory effect. The present stamp tax on deeds of conveyance was extended through June 30, 1941 by the Revenue Act of 1939, Section 1.[3]

Determining Factors in Land Valuation

Development of the revision of this device to make it appropriate and effective for our purpose can probably best be approached by a consideration in general terms of what influences and factors appear to determine the actual selling price of farm land as distinguished from what might be called its "normal productive value." The actual market value of a tract of farm land is in general determined by three sets of forces: (1) expectations as to future income to be derived from utilization of the land; (2) expectations as to the future course of the rate of interest; and (3) expectations as to future changes in the price of farm land itself.

The forces which together determine agricultural land values may be outlined as follows:

MARKET VALUE OF AGRICULTURAL LAND

I. Expectations as to the future income from use of land.
   A. Market's estimate of quantity and quality of land.
      1. Actual existing quantity and quality of land.
      2. Estimated future changes in amount or productivity of land.
         a. Anticipated income to be derived from land use.
         b. Expected future course of the rate of interest.
   B. Expected future level of agricultural prices.

II. Expectations as to the future course of the rate of interest.
   A. Actual going rate of interest.
      1. Quantity of money.
      2. Psychological liquidity preference.
   B. Estimated or expected changes in A1 and A 2, above.

III. Expectations as to future changes in the level of farm land values.
   A. Predicted changes in the level of agricultural income and the rate of interest.
   B. Combined individual estimates as to what other individuals will estimate to be the future course of land values.[4]

[3] Public Law 155, 76th Congress.

[4] Mr. Keynes, in discussing the stock exchange, char-

(*Footnote 4 continued on page 23*)

The Pervading Influence of Psychological Attitudes

From this maze of highly complex and interrelated forces one circumstance stands out. Of all the conditions which affect the market value of farm land only three are overt physical facts: (1) the existing quantity, in area, of available farm land; (2) the actual productivity at present of the available land; and (3) the quantity of money available to satisfy the liquidity motive. All other factors which influence the market value of land are subjective frames of mind on the part of an, at best, poorly informed populace. Liquidity preference and expectations as to the future of the rate of interest and the prices of agricultural products, and as to the speculative estimate of the future of land values themselves, are all subject to the whim and impulse of a great number of persons, very few, if any, of whom have any exact knowledge of the real factual basis for making correct estimates of the value of land which can be maintained over a long period by the actual productive performance of that tract of land.

It is the extent to which the sales prices of farms reflect group misrepresentation of economic conditions that seems to be the harmful element in the farm land market. To segregate farm land speculation from bona fide investment and from purchases by operating farmers is, of course, very difficult. Although, for theoretical purposes, unambiguous definitions could be framed, it is doubtful whether the material content of the operational concepts would be usable in empirical investigations.

(*Footnote 4 continued from page 22*)

acterized this factor as being very similar to a contest in which the most beautiful girl is picked by popular vote. Prizes are given to those persons who predict most closely the beauty rating given by popular vote to the girls in the contest.

Essential Requirements for a Device to Control Land Speculation

The major evil to be abated is the financial difficulty of farmers who buy farms at excessive purchase prices. The basic purpose of the device which should be developed is, therefore, to stabilize farm land sales prices at a level determined by the long-time earning capacity of the land. As has been pointed out, the failure of farm land prices accurately to reflect economic conditions is a result of the pervading influence of largely irrelevant psychological attitudes and frames of mind. The device used to prevent speculative land booms must provide an effective procedure to curb this propensity of people to be overly optimistic in judging fairly bright prospects for the immediate future.

In part, this problem is only a portion of the larger one of developing techniques to control the rate of interest and the level of investment. However, in a somewhat less than automatically operating economic system, a considerable amount of time may be required for the results of changes in one part of the economic system to be transmitted to others. For this reason and because psychological influences pervade every economic transaction, regardless of location, a direct treatment of the specific transaction (buying and selling in the land market in this case) appears to be required. If the points of view thus far presented are correct, it follows that the device for discouraging a speculative boom in farm land values as a result of the present or some future war or of any other condition must (1) deal directly with the transactions of the farm land market and (2) must be one which will result in the effective dampening down of overzealous psychological estimates of future income and profits.

Although the straight transaction or sales tax on land transfers as established under the stamp tax on deeds of conveyance has considerable merit if the rate of the tax is made high enough to be effective, it is likely that the advantages of this device can be combined with a capital gains tax to good effect. A capital gains tax to effect the control of land speculation was recommended by the President's Committee on Farm Tenancy:

"As a further means of controlling speculation, it is recommended that the Federal Government at an early date insert a provision in the Federal income tax law imposing a specific tax on capital gains from sales of land made within 3 years from the date of purchase. Due allowance should be made for improvements, including soil enrichment, beautification, reforestation, or other enhancement of value brought about by the owner. A capital gains tax, taking a large percentage of the unearned net increment, would materially discourage buying land merely for purpose of early resale, and would tend to keep land values on a level where farmers could better afford ownership. Special safeguards should prevent evasion through fictitious forms of ownership, and also prevent the tax working severe hardships in cases of unavoidable resale."[5]

By this procedure each transfer of agricultural real estate would be subjected, as at present, to a federal tax; the proposed amendment would provide that this tax be graduated in two directions: an increased rate of taxation (1) as the length of time since the previous transfer took place became less, and (2) as the percentage increase in the sales price of the land over the next preceding transfer increased, with allowance for the unexhausted value of improvements made during the period.

[5] *Farm Tenancy*, Report of the President's Committee prepared under the auspices of the National Resources Committee (Washington: Government Printing Office, February, 1937).

The Graduated Land-Transfer Stamp Tax Plan

The proposed revision of the existing tax involves a change in the method of calculating the rate and the amount of the tax as applied to agricultural land transfers. There is no necessity for change in the method of assessing the tax or in the administrative determination of which transfers are and which are not subject to taxation. The device envisioned under the proposed amendment would operate in the following manner. As under the existing legislation, a farm owner who desired to sell and had a buyer for his farm would first complete the transfer arrangements with the buyer; the seller would then apply, as he does now, to the Bureau of Internal Revenue, either directly or through the Post Office Department, for a land transfer stamp of the appropriate denomination. Determination of the cost of this stamp (its denomination) would be made from a simple table of rates on the basis of the sworn statement of the seller, or his agent, and of the buyer, or his agent, as to the validity of the data submitted for calculation of the tax. Any falsification of information in the sworn statement would be subject to a penalty of fine and imprisonment. This procedure would make it desirable for both buyer and seller to present fully, truthfully, and accurately the information needed for determining the tax rate and levying the tax.

Information needed from the seller includes: (1) the purchase price of the farm at the preceding transfer; (2) the unexhausted value of improvements made since the next preceding transfer; (3) the price for which the farm is now being sold; and (4) the date of the previous transfer. The buyer should be required to concur in the statement of the

seller concerning the present sale price of the farm. This information would be used in conjunction with a schedule similar to the one shown in Exhibit I to calculate the rate and the amount of the tax.

EXHIBIT I. SAMPLE SCHEDULE FOR CALCULATING RATES* OF TAXATION FOR THE SALE OF LAND TRANSFER STAMPS

Years since Previous Transfer	Present Sales Price as a Per Cent of Previous Sales Price					
	100–120%	120–140%	140–160%	160–180%	180–200%	200% or over
20 or more	0	2	4	6	8	10
10–20	4	8	12	16	20	24
5–10	10	16	22	28	34	40
2– 5	16	24	32	40	48	56
2	24	32	40	48	56	64
Less than 1	40	50	60	70	80	90

* The percentages shown in this schedule are merely illustrative. They do not necessarily represent the author's opinion of a correct rate schedule. A flat fee of $2 would be assessed for transactions in which no increase in sale price had occurred from one transfer to the next. It is mainly with respect to the substitution of this method of determining the rate and amount of the tax for the flat 50 cents per $500 or fraction thereof of transferred equity in farm real estate that the proposed plan differs from the present stamp tax on deeds of conveyance.

Two examples will make this process clear. On January 1, 1940 Landowner A desires to sell a farm and has made arrangements to effect the transfer with Buyer B. A submits the following sworn statements, with which B concurs in another sworn statement, to a representative of the Bureau of Internal Revenue and expresses a desire to purchase a land transfer stamp of the appropriate denomination:

Sale price in next preceding transfer.....$2,000.00
Unexhausted value of improvements made to land since next preceding transfer....$ 150.00
Sales price in present transfer.....$4,300.00
Date of present transfer.....January 1, 1940
Date of next preceding transfer.....July 1, 1939
The BIR representative would calculate thus:
$2,000+$150=$2,150
$4,300÷$2,150=2.00×100=200%
$4,300−$2,150=$2,150

July 1, 1939 to January 1, 1940 is less than one year. Looking down the column headed "200% or more" in Exhibit I, the clerk would stop at the line tabbed "Less than 1" and read from that cell, "90%," the rate of the tax. Multiplying, then, $2,150 by 90% would give $1,935, the amount of the tax or the denomination of the land transfer stamp required for the real estate title transfer.

In another example Landowner A and Buyer B submit the following information in their sworn statements:

Sale price in next previous transfer.....$10,000
Unexhausted value of improvements made since next previous transfer.....$ 500
Sale price in present transfer.....$15,750
Date of present transfer.....February 1, 1940
Date of next previous transfer.....March 1, 1932
Calculation:
$10,000+$500=$10,500
$15,750÷$10,500=1.50×100=150%
$15,750−$10,500=$5,250

March 1, 1932 to February 1, 1940 is 7 years and 11 months. Looking down the column headed "140–160%" to line 5–10 years, the rate of the tax is 16%. Then $5,250×16%=$840, the amount of the tax, or the denomination of the land transfer stamp required for the title transfer.

An alternative proposal which would effect almost identical results would be a provision for a flat capital gains tax which would allow deductions for past taxes paid by the seller to state and local governments. Thus all land transfers would be subject to a capital gains tax of, e.g., 95% with deductions allowed for all real property taxes paid to any governmental unit or agency. That the net effect of this tax would be similar to the preceding proposal will be clarified by an example.

In the case of the transfer examined in the first example, the capital gain is $2,150; $2,150.00×95%=$2,042. Suppose that real property taxes in the amount of $93 had been paid; $2,042 −$93=$1,949, or approximately the amount of the tax as figured by the rate schedule shown in Exhibit I.

Let us suppose now that the property had been held almost 10 years, instead of less than 1 year. The amount of real property tax paid would probably have equaled approximately $930.

The rate of the tax as figured by the schedule in Exhibit I would in this case be 40%. The amount of the tax as calculated by the rate schedule would be $2,150×40%, or $860. This is somewhat less than the $1,935.00−$930, or $1,005, the amount of the tax as figured by the second alternative proposal.

These two methods of taxation could be combined to good advantage by a provision whereby the total tax would be calculated from a schedule similar to that illustrated in Exhibit I, with allowable deductions for payments made on real property taxes during the period of ownership. In essence, this revision of the initial proposal would, in effect, result in increasing the steepness of the graduation as it applies to the length of the period of ownership preceding the transfer.

Administrative Considerations

The inauguration of this device as an amendment to the existing tax on conveyances would bring many administrative advantages over the inauguration of an entirely new regulatory device. No new administrative agency would be required since the proposed device could be executed by the Bureau of Internal Revenue which already administers the stamp tax on deeds of conveyance. Tax assessment and payment would be accomplished, as they are now, in one transaction by taking the sworn statements of the buyer and the seller prior to the sale of a land-transfer tax stamp to the seller.

The provisions of the existing legislation have been given. In administering this tax the Bureau of Internal Revenue has found it necessary to establish 45 regulations concerning various administrative details of the tax. Many of these regulations would be applicable to the administration and enforcement of the proposed revision.

Article 75 of these regulations states:

"The Act requires that the person who makes, signs, or issues any instrument taxable thereunder shall affix and cancel the revenue stamps. It also prohibits any person from accepting such instruments unless they are properly stamped."

This regulation appears to be appropriate for the administration of the proposed amendment.

The provision of Article 83 of these regulations would be essential to the effective administration of the proposed land transfer tax. This regulation reads:

"In the case of an exchange of two properties, the deeds transferring title to each are subject to tax, which should in each case be computed on the basis of the actual value of the interest or property conveyed, the amount of any preexisting lien or encumbrance which is not removed by the sale being deductible."

Article 84, defining real property, would of necessity have to be changed to define "agricultural real property."[6]

Other regulations are concerned with determining which transfers are and which are not subject to the tax. These provisions are shown in Exhibit II.

It is highly probable that a considerable number of further administrative regulations will be required to prevent evasion of the proposed tax. An obvious

[6] The ethical implications of this particularized treatment of agricultural land do not fall within the scope of this article. There appears to be no constitutional difficulty involved, inasmuch as the classification of land as between agricultural and non-agricultural is familiar and is likely to be considered as "reasonable" by the courts. Although the extension of the operation of a device of this nature into the fields of forest and urban land would result in an extension of its benefits to those fields, the consideration of the application of this tax to urban or to forest land is a subject in itself.

example of a type of evasion that must be prevented is the transfer of 99-year or other long-term leases. Article 108 of the regulations provides that leases of real property are not taxable. It will be necessary to amend this regulation. However, it should be pointed out in this regard that many states already have legislative prohibitions against extremely long-term agricultural leases, and in no state is a lease in perpetuity valid.

EXHIBIT II. CONVEYANCES WHICH ARE AND ARE NOT SUBJECT TO STAMP TAX ON CONVEYANCES

Type of Transfer	Subject to Tax	Not Subject to Tax
Conveyance of property subject to equity of redemption	x	
Conveyance of land in consideration of maintenance	x	
Deeds of building and loan associations	x	
Quit-claim deeds		x
Option and contract for sale		x
Deeds of release or trust		x
Tax deeds		x
Deeds conveying land to governmental units		x
Deeds to cover gifts		x
Deeds to trustees	x	
Deeds to building and loan associations	x	
Deeds to "straw man" by husband and wife		x
Deeds from agent to principal		x
Reconveyances of partnership property by receivers		x
Partition deeds		x
Deeds to confirm title		x
Conveyance by mortgagor to mortgagee	x	
Conveyances to or from a trustee		x

Enforcement of the tax would be insured, as it is now, by the provision for fine and imprisonment penalties on the seller and the buyer for falsifying their sworn statements or in any other way evading the tax. Administrative review of assessments and payments of tax could follow the already established procedure of the Bureau of Internal Revenue for checking compliance with the stamp tax on deeds of conveyance.

Local recording officers could be required by law to record no titles to which a land transfer stamp was not affixed. Although this action is not required by the present provision, it is reported that these local officials have been quite cooperative in requiring tax stamps on deeds and other titles before recording.

Although all administrative difficulties of this device cannot be forecast, it appears fairly certain that some difficulty is likely to arise in preventing tax evasion through the allocation of a fictitiously high value to unexhausted improvements. This difficulty could be reduced in two ways: (1) by not allowing the deduction; and (2) by strict administrative review and enforcement. Both from the economic and the practical standpoints it is clear that this deduction should be allowed. Therefore, it will probably be necessary to depend on strict enforcement of the tax to overcome this possibility of evasion.

Economic Effects of the Stamp Tax

The important regulatory features of the land transfer tax from an economic standpoint are the penalties on the rapid turnover in farm ownership and on the sale of farms at higher prices than those at which they were purchased. Will these features of the proposed amendment effect the required results? The primary result desired is the prevention of farm purchases at prices higher than "the normal productive value" of the land. Moreover, the effect of the law should not be such as unduly to burden justifiable farm land transfers or to place unnecessary handicaps of any kind on bona fide operating farm owners. It has been pointed out earlier that the failure of sale prices to equal normal productive value of farm land is attributable to speculative activity grounded on the psychological propensity of market operators to be overoptimistic in their esti-

mate of prospects for the immediate future. The secondary objective of the plan should be elimination of the exploitative management of farm land frequently associated with a rapid turnover in its ownership.

It has been pointed out that the land-transfer stamp tax plan is a combination of a graduated capital gains tax with a graduated farm land sales tax. The specific economic effect of an ungraduated capital gains tax would be to remove from the farm land market a considerable amount of the speculative demand. If the graduated principle is combined with it, this tendency would be strengthened. The graduated capital gains tax would result in taxing away most of the large profits to be gained from the sale of farm land at a higher price. For real estate operators whose only interest in land is the possibility of sale at a higher price, most of the incentive to enter the market would be removed. For such operators land purchase is always more or less of a gamble since, as far as they know for sure, the price may go down. If the possibility of a large gain is removed, the wager becomes less attractive.

An ungraduated farm land sales tax, such as the stamp tax on deeds of conveyance, creates a burden of cost on all transfers alike. A sales tax graduated in indirect relationship to the length of the period of ownership would place an increasing burden of cost as the rapidity of ownership turnover increased. Under a land transfer tax, graduated or ungraduated, the land must be worth more to the buyer than to the seller by at least the amount of the tax. The graduation feature would penalize quick sales of land and would tend to reduce the number of such sales, thus effecting directly the secondary objective desired.

When a graduated sales tax and a graduated capital gains tax are combined, as in the proposed revision of the stamp tax on deeds of conveyance, it appears fairly certain that the desirable effects of both would be obtained. The double graduation principle would alleviate many of the objectionable features of each of these measures. As a land transfer tax, the proposed plan would place a burden of cost on certain types of land transfers; with the double graduation, quick sales with large profits would be forced to carry a heavier burden than sales made after a long ownership with little increase in price over preceding sale. It appears fairly certain that the land-transfer stamp tax would effectively remove speculative demand from the land market. In the terminology of the economic theorist, this lessening of force on the demand side of the land market would cause the demand curve of "land for purchase" to shift downward and to the left with the result that, other conditions remaining unchanged, the exchange prices of land would fall.

To this extent the proposed tax would tend to effect the realization of the primary objective listed. It appears, also, that the proposed tax would result in discouraging overoptimistic prospective farm operators from bidding too much for the land purchased because of any inflated expectation on their part as to the future course of agricultural prices. There appear to be two ways in which the proposed plan would affect these bona fide buyers of farm land. In the first place, the lack of speculative demand in the land market would substantially dampen psychological overoptimism on the part of farmers, and would, thus, tend to make them more realistic in their purchases. Secondly, as was pointed out earlier, if the land to be purchased by such a buyer were being held for a higher price than that at which it was purchased, a sale could not be consummated except as the buyer were willing to pay a

price greater by the amount of the tax than that at which the seller desired to sell. These same influences would also tend to prevent the speculative purchase of land by prospective landlords.

On its face the proposed plan may seem to involve some danger that it might result in the development of a permanent land owning class who would rent rather than sell their land, thus avoiding the transfer tax. This danger appears, however, to be fictitious upon closer examination. It is highly probable that the effective removal of speculative owners from the land market would result in a lower rather than a higher prevalence of tenancy. Moreover, there appears to be no reason why the proposed tax, graduated as it is in indirect relationship to the length of previous ownership, should tend to deter the sale of farms from older to younger farmers. The proposed tax appears to contain nothing which would affect one way or the other the desire or ability of present "permanent" landlords to be tenacious in their ownership. If they have owned the land for a considerable period, they would realize almost the whole of the sale price if they sell; the tax would thus not tend to discourage the sale of farm land by such owners.

Another corollary effect of the tax must be considered. What will be the effect of the proposed plan on the credit position of present and prospective owner-operators of farms? If the tax should result, as appears most likely, in sales prices of land more closely following its long-time earning capacity, the security of long-term farm credit should be increased. Greater value stability should, in turn, result in more liberal lending policies by credit institutions, thus increasing the ability of prospective owner-operators to obtain the necessary credit with which to purchase the needed farm land. Bringing farm land prices into a closer alignment with the normal earning capacity of the farm should increase the ability of farm operators to pay their debts, thus again increasing the security of long-term agricultural credit.

Although the proposed tax would probably result in a lower level of land values, and thus a smaller total amount of collateral for mortgages, it should be remembered that the lower farm land price levels would also mean that farms could be purchased at lower prices, and thus less credit would be required for land purchases. Moreover, it should also be noted that with greater security a higher proportion of the value of the land could be safely advanced on the collateral of a mortgage. In this regard, credit agencies would be affected by the tax, in the case of foreclosure, only if they should resell the farm for a sum greater than the previous purchase price, that is the amount of the indebtedness for which they foreclosed. In this respect, the proposed land-transfer stamp tax would likely tend to reduce the number of unjustified foreclosures.

Legal Considerations

As a federal tax the land-transfer stamp tax plan appears to have a good chance to be upheld constitutionally. There appear to be well established precedents for considering a capital gains and excess profits tax as an income tax, the right to levy which is lodged in the Federal Congress. Moreover, the Supreme Court has held on occasion that the secondary effect of a tax to regulate economic activity will not invalidate a tax, which in point of fact will produce some revenue. The power of the Federal Congress to tax land transfers is already established. The constitutional limitation against the taxation of real property is not effective in this case as the subject of the tax is the *transfer* and not the *property*.

Significant Post-Depression Changes in Savings and Loan Practices

By FRED T. GREENE*

STUDIES of the number and dollar-volume of mortgage loans recorded indicate that savings and loan associations are continuing as the largest single institutional source of mortgage credit on homes in the United States. Although comprehensive data are not available to show the mortgage loan volume of various types of lenders in the pre-depression decade, such figures as are available indicate that savings and loan associations attained their dominance in the home mortgage field in the twenties and have continued to be the largest single private institutional suppliers of home financing funds ever since.

During the first 11 months of 1939, it is estimated[1] that 1,249,553 home mortgages, totaling $3,449,054,000, were recorded in the United States. Savings and loan associations were responsible for a larger number of mortgages and a larger dollar-volume than any other single class of home financing institutions, with a total of 424,407 mortgages recorded by such associations. This represented 34% of the total number of mortgages. The dollar-volume of savings and loan mortgages during this 11-month period accounted for 31% of the total, or $1,072,351,000. Table I shows the estimated volume of home mortgage loans by all types of private lenders for the period 1929 to 1938 and for the first 11 months of 1939.

During the twenties and early years of the past decade, savings and loan associations were practically the only source of long-term, monthly amortized home mortgage loans and it is easy to understand how these associations obtained a large proportion of the mortgage business available during that time. The typical family can afford home ownership only if it is able to pay for the home on an amortized plan over a relatively long period of time. Beginning in 1934, and with increasing volume in succeeding years, other types of financial institutions began to emulate the practices of savings and loan associations by adopting the long-term, monthly payment home mortgage. This trend was given great impetus by the work of the FHA when it adopted the monthly payment long-term mortgage in its insured mortgage program.[2] The dearth

TABLE I. ESTIMATED VOLUME OF MORTGAGE LOANS MADE ON NON-FARM, 1-TO-4-FAMILY DWELLINGS, BY PRIVATE LENDERS, 1929–1939*
(Millions of Dollars)

Year	Savings and Loan Assns.	Insurance Co's.	Mutual Savings Banks	Commercial Banks	Individuals	Total
1929	$1,791	$525	$612	$1,040	$1,120	$5,088
1930	1,262	400	484	670	720	3,536
1931	892	169	350	364	400	2,175
1932	543	54	150	170	175	1,092
1933	414	10	99	110	100	733
1934	451	16	80	110	150	807
1935	564	77	80	264	443	1,428
1936	755	140	100	430	605	2,030
1937	897	232	120	500	723	2,472
1938	798	242	105	560	669	2,374
1939†	1,072	303	127	844	1,103	3,449

* *Seventh Annual Report*, Federal Home Loan Bank Board, June 30, 1939, p. 167, and Mortgage Recording Letters for 1939.
† First 11 months of year.

* President, Federal Home Loan Bank of Indianapolis.

[1] Estimates are based on mortgage recording studies made each month by the Federal Home Loan Bank Board.

[2] In this connection, see Frederick M. Babcock, "Influence of the Federal Housing Administration on Mortgage Lending Policy," 15 *Journal of Land & Public Utility Economics* 1–5 (February, 1939).

of commercial loans acceptable to commercial banks and the lack of attractive investment opportunities open to life insurance companies turned the attention of these two great classes of financial institutions to the long-term, monthly amortized home mortgage loan. This influx of vast amounts of new funds into this field has resulted in extremely competitive conditions in the type of mortgage lending heretofore supplied largely by savings and loan associations.

Recent years have witnessed a number of important changes in savings and loan practices and procedures. The modernization of loan plans, adoption of newer loan merchandising methods, new accounting procedure, and the like have been hastened by the play of competitive forces upon the local thrift and mortgage institution. The purpose of this paper is to describe briefly the more significant of these changes.

Changes in Lending Policies

Direct Reduction Loans. The original building and loan associations formed more than a century ago were developed under a loan plan in which both investors and borrowers shared alike in the risks and profits of the association's lending operations. This lending plan worked remarkably well among the small cohesive groups of individuals comprising the early associations. Many savers and investors, however, began to accumulate funds for purposes not necessarily concerned with home ownership and many borrowers who sought home financing did not desire to wait until funds had been accumulated in their own group for the financing of home ownership. These circumstances led to the adoption early in the present century of what has come to be known as the "monthly direct reduction loan plan."[3] Savings and loan associations in some localities began to use this plan years ago but the plan did not attain wide adoption by associations throughout the country until the middle 1930's.

The direct monthly reduction loan plan is a simple one under which the monthly payments by the borrower are applied first to the interest due for the one month, with the balance of the monthly payment being used to reduce the principal of the loan. The result of the plan is to give the borrower a new loan balance each month. Interest is then paid only on the unpaid balance of the loan. This plan was used by the HOLC in its huge refinancing operations and was later adopted by the FHA. It is also being used by banks and insurance companies and the bulk of the current lending business of savings and loan associations is now on this plan.[4]

Flexibility of Loan Terms. Prior to the depression, it was common practice among mortgage lenders to have one or two fixed types of loan plans available to borrowers. This was true of savings and loan associations with their long-term plans as well as of other institutions which commonly operated with three- to five-year straight loans. Typically, savings and loan associations offered the borrower a loan with a fixed monthly payment. Seldom in the past were attempts made to provide a "tailor-made" repayment schedule based upon the borrower's income. Complications in the typical loan plans in vogue in past years made it difficult for many savings and loan associations to offer a loan service with the complete flexibility which is in common use among these institutions today. A great majority of

[3] A New York City building and loan association advertised the direct reduction loan in 1900 under the name of "The Twentieth Century Loan Plan."

[4] *Seventh Annual Report*, Federal Home Loan Bank Board, *op. cit.*, p. 85.

the active lending associations today are able to offer monthly repayment terms to fit the needs and circumstances of the individual borrower, taking into account, of course, the age, construction, and location of the home to be refinanced.

This flexibility is providing a more desirable type of financing for individual families and at the same time is increasing the number of borrowers whom these associations can serve safely. The philosophy of most savings and loan officers and directors is, however, to encourage as rapid amortization of loans as a family's income will permit rather than to extend the loan payments over the maximum years available merely for the sake of low monthly payments. Such a philosophy has two definite social advantages. It tends to encourage debt-free home ownership at an earlier period than is possible when payment plans are stretched over an unnecessarily long period of time and it tends to encourage families to live in homes more in keeping with their income.

Variable Interest Rates. A third recent development in savings and loan lending operations has been the adoption of variable interest rate plans. This type of program represents an adaptation of a principle long used in other types of credit extension—namely, the smaller the risk involved in a given loan, the lower the rate of interest such credit transaction can command. Historically, one of the fundamental purposes of savings and loan associations has been to finance homes for people of medium and small incomes. As a matter of fact, until recently the typical workingman's family had practically no other source of home financing than these associations. The purpose of the variable interest rate plan is to permit an association to serve families and homes in all economic levels of the community. Loans which are small in proportion to the value of the house, which are on well located properties, and on which the monthly payment involved represents only a small proportion of the income of the borrower, can be financed at low rates of interest because the risk involved in such transactions is low.

On the other hand, a great segment of the population have small incomes and are forced by circumstances to live in less desirable neighborhoods. People in these circumstances are entitled to home financing but, because of the risk involved, it is necessary for lenders to build up larger reserves to take care of possible losses. In such transactions, collection and bookkeeping costs are likely to be larger. These loans can and should command a slightly higher rate of interest to offset the greater cost of handling and the greater risks involved. The variable interest rate plan includes a rating device which attempts to gauge impartially the risk in each given loan, taking into consideration all factors affecting risk, such as type of construction, age of property, location, and the moral and financial risk elements inherent in the borrower. Use of variable interest rates by a large number of savings and loan associations is permitting them to make a larger volume of loans than could be made on a sound basis without such a program.

Monthly Collection of Taxes and Insurance. One of the most important innovations in savings and loan practice has been the inclusion in the monthly payment by the borrower of an amount to cover 1/12 of the annual taxes and 1/12 of the annual hazard insurance premium paid to protect the physical property. Depression experience indicated that one of the most important factors causing defaults in loans is the inability on the part of the average

family to accumulate lump sums with which to meet tax payments as they come due. Savings and loan executives had long recognized this problem and in some localities had provided a form of installment savings share account for accumulating sums with which to meet these large annual or semi-annual payments. From this type of program came the idea for the systematic collection of taxes and insurance each month as a part of the total payment by the borrower. This program has been adopted by numerous savings and loan associations and has become most attractive to the borrowers.

Increased Service to Borrowers

Construction Loan Service. Historically savings and loan associations have provided financing for new construction but much additional attention has been given to this phase of service by savings and loan associations in recent years. A number of associations have established a construction loan department with a trained construction loan personnel. Where such service has been fully developed, it typically includes a plan service and in some instances a building materials exhibit, facilities for accurate estimation of construction cost, architectural inspections of plans and construction during the various stages of building, with disbursements in installments upon completion of certain specified steps in the building of the home. In view of the fact that the typical borrower seldom builds more than one home in his lifetime, this type of service has been welcomed by the public and has resulted in the associations' attaining a larger number of good loans which otherwise might have been financed elsewhere. An interesting feature of the construction loan service has been the device of postponing the first amortization payment for periods up to six months after completion of construction, thus permitting the borrower to meet other expenses which always arise with purchase of a new home.

Prompt Commitment Service. A high degree of emphasis has been put on prompt commitment service on loan applications by savings and loan associations. These associations are locally owned and are managed by a local board of directors; therefore, they are usually able to give much more prompt action on loan commitments than are lenders whose managements are located in other cities. A synchronization of the association's loan application department with the obtaining of credit reports, appraisals, and inspections has been attained, permitting loan committees of the associations to obtain all essential information and facts regarding loan applications in a rapid manner so that firm commitments can be extended to the borrower within a very reasonable period of time. In cases involving construction, the associations which have developed a complete construction loan service have likewise been able to obtain a thorough check of plans, specifications, and cost estimates quickly. The majority of savings and loan associations operate within a small radius of their home office and because of this localized nature of their work are usually thoroughly familiar with the neighborhoods, trends, and conditions of the area which they serve; and in many cases, particularly in the smaller communities, are familiar with the individual properties and individual citizens of the community, all of which facilitate rapid and at the same time thorough consideration of the elements which determine the quality of a given loan application.

Accessible Offices. One of the marked trends in the savings and loan business

in recent years has been the establishment of association offices in locations more accessible to a large number of borrowers and arranged to attract a larger number of potential customers. This trend is particularly a result of competitive conditions which have forced the associations to seek locations which will bring in potential borrowers in much the same way that a well located retail store will bring in prospective customers. This trend is also partially the result of the considerable number of mergers and consolidations of associations which have taken place in the recent past and which have created a larger average size of association with larger operating incomes for such purposes.

This trend to more accessible and attractive offices has been accompanied by greater merchandising efforts and larger expenditures for advertising the loan service of associations. Better locations for association offices is a natural outgrowth of the fact that these institutions are now serving a wider segment of the public rather than being confined to homogeneous groups of people brought together by ties other than the desire for either a safe investment or a sound home financing plan.

Acceptance of Prepayments without Penalty. One of the underlying philosophies of the savings and loan business is the encouragement of debt-free home ownership. In line with this fundamental purpose of the association it is common practice in many of these institutions to permit the prepayment of loans in full or in part at any time without penalty. Permitting the borrower to repay loans without penalty has proved helpful in numerous cases where borrowers, who from one source or another may receive lump sums of money, have been permitted to apply these sums against their mortgage debt rather than making other uses of the money. The borrower has thus reached his objective of debt-free home ownership more rapidly than his original program contemplated.

Life Insurance Protection for the Borrower. Some savings and loan associations are currently offering a low-priced type of life insurance protection to the borrower which will immediately liquidate the mortgage obligation for the family in case the head of the family dies. Several life insurance companies have devised a special form of life insurance policy for this purpose and are offering the protection to savings and loan associations' borrowers. Usually the life insurance protection is in the form of a reducing. term insurance policy based on a schedule of protection which decreases as the loan is amortized. The advantage of this particular type of insurance is its low premium cost. Some companies have arranged for a single premium, the amount of which is added to the loan and amortized monthly by the borrower.

Improvements in Investment (Savings) Functions

Attraction of Funds. Savings and loan associations are primarily dependent for their loanable funds upon the accumulations of private savers and investors and this, in order to fulfill their function of providing home financing, must at the same time encourage thrift savings and investment. Recently a number of changes have been made in the investment side of savings and loan operations in order to permit these associations to attract funds not only in volume but at a relatively low cost. The principal changes of this type include the adoption of the so-called "non-serial" type of savings and loan plan whereby investors and savers can begin their periodic investments in the association at any time as contrasted

to the "serial" form of investment program common in the past.

Another important factor in the attraction of a large volume of low cost funds has been insurance of accounts provided by the Federal Savings and Loan Insurance Corporation which insures savings and investment accounts in savings and loan associations against loss up to $5,000 for each investor.

The facilities of the Federal Home Loan Bank System, which acts as a credit reservoir to provide funds to associations for lending or liquidity purposes during those periods when sufficient funds for either purpose are not being attracted locally, has also proved an important factor in enabling savings and loan associations to attract funds from the public and to make new loans. Currently, the associations are obtaining a sufficient volume of new savings and investments from the public[5] to maintain their position as the dominant institutional source of home financing funds on small homes of the nation.

These changes in practices have been taking place in associations throughout the country at a rapid pace. The federal chartering of savings and loan associations, resulting in the establishment of more than 1,300 associations with uniform charters and close similarity in practices and procedures, has had great influence in bringing about these improvements. Dividend rates paid to investors and savers in the associations have trended downward from the 5% and 6% rates common in the past to 3%, 3½% and 4% prevalent today. In some of the financial centers in the East, dividends have been reduced to 2½% per annum. This reduction in dividend rates has come about largely through the reduction of the gross return to associations because of their reduced interest charges to borrowers. Reductions of this kind in costs of mortgage money and in returns to investors are in line with the trends in other financial institutions.

Commonly, the downward trend in rates to investors has resulted in a wider spread between the cost of money, represented by the association's dividends, and the selling price of the money, represented by interest costs to the borrowers. Typically, the spread obtained today is from 2% to 2½%. It is not possible to compare directly today's margin with the margins existing in the past because of differences in loan plans and accounting methods used. However, it appears that a modernized savings and loan association is able to operate on as favorable an overall expense basis as in the past.[6]

The associations are using the increased margin to build up larger reserve positions than were common in the past. The tendency toward building up larger reserves has grown out of depression experiences. Recent changes in many state laws have both permitted and required larger accumulations of reserves in the associations.[7] At the end of 1938, the 3,895 member associations of the Federal Loan Bank System had reserves and undivided profits equal to 7.18% of assets. This is a large accumulation of reserves in view of the fact that the laws of many states, prior to the depression, encouraged associations to distribute all their earnings directly to members with only

[5] Private share capital in savings and loan associations which are members of the Federal Home Loan Bank System is increasing at approximately 10% a year. (*Seventh Annual Report*, Federal Home Loan Bank Board, *op. cit.*, p. 79.)

[6] Total operating expenses of 3,094 reporting member savings and loan associations of the FHLB System for the year ending December 31, 1938 were 25.94% of the gross income of the associations. The comparable figure for the year 1935 reveals that total operating expenses were 23.67% for that year for 2,553 associations. Similar data are not available on a comparable basis for earlier years.

[7] *Seventh Annual Report*, Federal Home Loan Bank Board, *op. cit.*, p. 87.

nominal accumulations of reserves and undivided profits accounts.[8]

The accumulation of reserves and undivided profits in the associations is having three important effects upon the operation of these institutions: (1) it is making the associations more attractive to investors and thus enabling them to obtain funds at lower cost; (2) it is contributing to the associations' ability to adopt the innovations necessary in today's competitive lending because of the earnings on the reserves, part of which are commonly invested in mortgage loans; and (3) it is encouraging the carrying of larger liquidity positions because managers of the associations feel less pressure to have all their funds invested when a portion of their capital is represented in reserves and undivided profits upon which accounts no dividend accrues. In the old time, community-type savings and loan association, management took great pride in keeping the liquidity of the association at the smallest possible figure. Today, cash positions of from 5% to 10% of the associations' assets are not at all uncommon.[9] The increased liquidity of savings and loan associations has been another factor in enabling them to attract new savings and investments in volume because of the confidence which increased liquidity instills in the minds of investors.

Another betterment in savings and loan operations, in line with the improved accounting procedure adopted by many of these institutions, is the improved quality of auditing, examination, and supervision on the part of the various state governments and of the Federal Government through the Federal Home Loan Bank Board, the Federal Savings and Loan Insurance Corporation, and the 12 Federal Home Loan Banks. Improvements in auditing and examining techniques are proving helpful to managements and directorates, both in the procedures of operation and in many important phases of policy.

Implications of These Changes

The current progress of savings and loan associations in fulfilling their functions as suppliers of long-term home-financing credit in the country appears likely to continue. These associations seem destined to become more important in the nation's financial structure. The legislative framework upon which these associations are built in the several states and nationally has been strengthened in a way that encourages the sound development of these institutions. They are in a better position to serve the public than at any time in their history through the improvements in their procedures, operations, and policies, and the greater flexibility now provided. These associations which historically were developed as small community enterprises are, through the changes briefly described, taking on the attributes of major financial institutions. They are attracting a new type of investor, including individuals of large means and corporations, as well as maintaining their service for the small saver and investor. The increase in investment funds which these associations are attracting and the betterments in their procedures and policies are resulting in widening service to home owners in specialized long-term home finance. All indications are that these trends will continue.

[8] It is estimated that combined reserves and undivided profits represented less than 1/2 the proportion of assets in 1929 that they do today.

[9] Cash and investments in the 3,895 member savings and loan associations of the Federal Home Loan Bank System as of December 31, 1938 accounted for 7.21% of associations' combined assets.

The Wisconsin Telephone Case

By MARTIN G. GLAESER*

WHEN, in 1931, the legislature of Wisconsin undertook the reorganization of the old but justly famous Railroad Commission, by refurbishing its old powers and conferring upon it certain new ones, the vigor with which the newly staffed Wisconsin Public Service Commission took hold of its administrative duties augured well for the future of public utility regulation in the state in which, among a select few, this policy had been cradled. The cause celebre, testing out this administrative new start, was the state-wide investigation, begun July 29, 1931 on the commission's own motion, of the rates, rules, services, practices, and activities of the Wisconsin Telephone Company.

After eight years of effort by the commission and the expenditure of nearly two millions of dollars by a conscientious and efficient staff, the Wisconsin Telephone Company case has come to rest with the affirmation on July 11, 1939 by the Wisconsin Supreme Court of a judgment by the Circuit Court of Dane County, setting aside as unreasonable and unlawful a temporary rate order of 1934 and a final rate order of 1936.[1] Optimists can, perhaps, extract some slight comfort from the fact that in a separate opinion the Supreme Court upholds a commission order fixing a composite depreciation rate for this company.[2] It should be stated that during this period there were issued three opinions and interlocutory rate orders reducing exchange rates: the first two ordering a reduction of 12½% were effective for one year each after August 1, 1932; the third ordering a reduction of 10% was effective for one year. The final order reducing rates by 8% was effective May 1, 1936. Only the last two were considered in this appeal, the first two having found their way into the federal courts. Unless the Supreme Court of the United States can be persuaded to grant a further appeal to the commission, the hope of obtaining an adjudication by that body of the very important issues raised in these proceedings has gone glimmering.[2a] It is one of the anomalies in this decision that, although the trial court found that the prescribed rates were confiscatory, the judgment of the trial court and the opinion and decree of the Supreme Court did not find that the rates fixed were confiscatory but only that the orders were "unreasonable and unlawful."

At the outset, Chief Justice Rosenberry classifies the questions presented upon appeal: (1) those relating to procedure and due process; (2) those relating to the merits of the case, that is to say, the rate-base, the fair rate of return, and the income of the company.

Procedural Aspects

On the question of procedure the court says that the primary function of Wisconsin state courts in reviewing commission rate orders is not to consider confiscation but to set these orders aside if they are found upon clear and satisfactory evidence to be unlawful or unreasonable. In this connection the court notes this distinction:

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[1] *In Re State-wide Investigation of Wis. Tel. Co.*, W.P.S.C., March 24, 1936; *Wis. Tel. Co. v. Pub. Serv. Com. of Wis.*, 287 N.W. 122 (July 11, 1939).

[2] *Wis. Tel. Co. v. Pub. Serv. Com. of Wis.*, *supra* n. 1.

[2a] This Court has refused to review the order on the ground that no federal question is involved.

"When the Legislature itself has prescribed a rate by an act duly and regularly adopted, that rate may be assailed only on the ground that the act is confiscatory in its nature. When, however, the Commission establishes a rate, its act must not only be non-confiscatory but it must have been established in the manner prescribed by the Legislature . . ." (p. 131).

In making the temporary rate order the commission was proceeding under statutory provisions empowering it to issue conditional, temporary, emergency, and supplemental orders. The court finds, however, that what a commission may do

"upon the application of a utility in the way of *increasing* rates *under emergency conditions* is no measure of its power to *decrease* rates under similar conditions. Assuming that a rate is higher than a just and reasonable rate as a matter of law, the public is not deprived of its property because it has an option to accept or decline the services. When, however, an unreasonable rate is established the property of the utility is taken because under the law it has no option to render or decline to render the service" (p. 133). (Italics supplied.)

In this case the commission was fixing rates without the consent of the utility; therefore, it had to give the utility a full and fair hearing. This the court finds, after reviewing the history of the case, the company did not have as to the temporary rate order. In view of the importance of temporary rate procedures, it is interesting to note some of the other reactions of the court. "Even by way of test or experimentation the state may not confiscate the property of a citizen." If experimental rates result in a loss to the utility, statutes like those enacted by New York and Pennsylvania, providing for a procedure for amortizing the loss, "point to a solution of this difficult and perplexing problem. Under such statutes rates may be based upon experience rather than upon prophecy and guess work." And again, "when rates are increased upon the application of the utility, the Commission consents for the people and the resulting order is in effect a consent order. When rates are decreased upon application of the utility, a like consent order results if the commission approves the license." It seems a commission is in loco parentis of the public but not of the utilities.

In general, the history of this case is replete with acrid criticism of commission procedure. The lower court was particularly incensed. Even the final order, though not questioned on the score of the company being accorded a full hearing, "was issued without a fair hearing and with such bias and prejudicial conduct by the commission that the order deprives the plaintiff of property without due process of law, etc."

What particularly irked the lower court was that staff members who were also witnesses should be found preparing and writing portions of the opinion. Fortunately for the future of regulation in Wisconsin, the supreme court was able to dodge behind a legalistic interpretation of the functions of a technical staff. We quote:

"The Commission may not abdicate its power or delegate its fact-finding function to material witnesses. In cases, however, involving special or technical problems, the Commission may without depriving a party of due process or a fair hearing delegate to members of its staff even though they have been material witnesses the duty of putting into proper form and technical language its findings upon engineering and accounting questions. There is no reason to suppose that the contribution of the witnesses to the findings was any more than that of casting them into technical language appropriate to the disposition of accounting and engineering problems. This function the Commission was doubtless unequipped to perform. We conclude that the use of the technical staff in this way infringed no constitutional rights of the Company and constituted no violation of the

statutes, although where this procedure is adopted the doctrine of the *Morgan case* does apply and notice of the findings should be served upon the Company and an opportunity be given for an argument on the basis of these findings. This right was accorded to the Company when the rehearing was granted and the matter reargued" (p. 143).

Another important pillar of administrative regulation called into question in this proceeding is that which accords to findings and determinations of the commission the presumptions of prima facie reasonableness, thereby placing the burden of proof upon the adverse party. The trial court found that this presumption had been destroyed because the commission failed to give a fair hearing. In reviewing this branch of the case, the court said:

"We come now to a consideration of how the bias and prejudice found by the trial court affects the weight to be given to the findings and determination of the Commission. An examination of this question imposes upon this Court a duty of a disagreeable nature but one which it must discharge. In the beginning we may say that we acquit the Commission of any intentional disregard of the rules of law which govern its actions. It seems to us that the Commission entered upon this inquiry in a state of mind induced by the existing depression which more or less subconsciously led it to a position where it was very difficult, if not impossible, for it to give a dispassionate judgment upon the facts. Prior to the issuance of the 1932 order and apparently as a basis for the whole investigation, the Commission brought before it a number of nationally known economists, among whom were Dr. F. C. Mills, Dr. E. R. A. Seligman, Dr. Frank A. Fetter, Dr. C. K. Leith and others. The economists gave a large amount of testimony relating to general economic conditions, their cause and probable effect and on the basis of that testimony arrive at certain underlying conclusions. Among other things the Commission in the 1932 order said [p. 124]: 'The present depression is no minor disturbance. It constitutes an economic crisis of major proportions. . . . There are facts in the record relating not only to the country as a whole but especially to Wisconsin farmers, wage-earners, corporations, and citizens generally. These are the customers of the utilities under our jurisdiction.

" 'When their incomes on the average have shrunk by 25% or more, when less than a third of Wisconsin corporations report taxable incomes, when farmers receive 50% less than in 1929, when all measures of wage-earners' livelihoods show unprecedented losses, we surely are not dealing with any minor disturbance. The prices of most commodities have been drastically cut, though in varying proportions. But utility rates and a few other prices have virtually stood still . . .' " (pp. 145–6).

Enough has been quoted to indicate the gist of the argument. The commission sought to prove that rates were being investigated at a time of supervening emergency, that in such times the question of the reasonableness of rates was not subject to the normal criteria of reasonableness. It was not basing emergency rates solely upon cost of service but upon value of service, since the commission referred also to that part of the rate-making rule of *Smyth* v. *Ames* which restricts the level of charges to no more than the services are reasonably worth. For this purpose the testimony of nationally known economists had been introduced. The commission was trying to prove, perhaps ineptly: (1) that a national economic emergency existed for which the commission had been granted emergency powers; and (2) that in a time of rapidly falling price levels, the value in terms of commodities of a relatively fixed monetary return would rise rapidly. Certainly that is evidence of some importance.

The court's argument is hardly convincing. It deplores the fact that the company's surplus would have declined from $9,401,483 on December 31, 1930 to $941,129 on December 31, 1936 if the rate reduction orders are sustained. In face of the general distress, the court

contributes this biased, inaccurate, and prejudiced observation:

"Nor do we find that the statute confers upon the Commission any power to relieve the economic condition of consumers by taking property away from the utility and awarding it to its patrons. What the statute authorizes the Commission to do after it has found that existing rates are unjust and unreasonable is to establish a just and reasonable rate which has been defined over and over again. If the Commission were empowered to review the whole internal economy of the state, its postulates and arguments might sustain the conclusion that it reached. Within the limits of its statutory authority, however, it had no right to give dominant weight to economic theory in the face of the statutory command. Recent years seem to have pretty thoroughly demonstrated that economic theory is vague, uncertain and undependable and that predictions based upon it are not reliable. It seems to be in constant need of repair and readjustment" (p. 147).

When the commission sought to prove that the expenditures of the company for operations were excessive and justified its efforts in this direction by calling attention to the fact that regulation had to do the work of competition, it was met by judicial assertions like the following: "No claim that the Company was recklessly and improvidently throwing away its funds is made." Can it be that the court is using "unreasonable" as synonymous with "reckless," "improvident," and "wasteful?" Economists and others interested in the workings of regulation should note this general characterization: "The philosophy of management embodied in the opinions of the Commission in this case would place the Company in a managerial straitjacket."

The court concludes this section of its opinion with this summary finding:

"We have set out enough to indicate that while the Company did not have a hearing of such a biased and prejudicial character as to deprive it of due process of law, the evident bias of the Commission and some of its principal witnesses and its disregard of fundamental principles underlying the valuations of public utility property in certain instances has been such as to require the reviewing court to scrutinize its determination with great care. Under such circumstances the evidence necessary clearly and satisfactorily to establish the fact that the findings of the Commission were wrong is much less than it would otherwise be and the force of the contention made on behalf of the Commission that the trial court did not give sufficient weight to the findings of the Commission is greatly diminished if not wholly dissipated" (p. 149).

The court pays lip homage to the idea, often announced, that it should not substitute its own idea of reasonableness for that of the commission, when it said: "If the rate established falls within the zone of reasonableness, it must stand even though in the opinion of the trial court or of this court the Commission erred and a more reasonable rate might have been found." Even though the court absolved the commission from the charge that its procedure in making the final order was not in accordance with the provisions of the statute, the following comment reveals to some extent the judicial animus: "While the Commission did not base the final order of March 24, 1936 upon the ground that an economic emergency existed, that it still clung to its economic theories is indicated by the opinion."

To this reviewer the present attitude of what was once a helpful court in establishing administrative regulation can only be intelligible on the hypothesis that the court is again unfriendly to the administrative process and wants to curb it. Conceding that the commission was unwise in signing the temporary order of 1933 "before hearing argument with respect to it and the systematic furnishing of advance reports to the press of what witnesses for the Commis-

sion were to testify to in a proceeding pending before the Commission," this, as the court itself points out, did not terminate the proceeding. Following the statute, after each of the four orders, "there were motions for rehearing, exhaustive specifications of claimed errors. The motions for rehearing were granted and at the rehearing the whole matter was reargued."

Recent decisions by our Highest Court have again brought this question of administrative procedure into the forefront of public attention. The old rule, derived from the Louisville and Nashville Railroad case, requiring commissions to base their orders only on evidence introduced at open hearings, corresponds to a judicial ideal. But the commission's functioning is not only quasi-judicial, it is also said to be quasi-legislative and quasi-executive. Could it be that the legal theory in this instance, like the economic theory which Justice Rosenberry does not like, is similarly "vague, uncertain and undependable," "seems to be in constant need of repair and readjustment." Even the background fact of the depression which began in earnest in 1931, if not the theories which seek to explain it, may come within the scope of judicial notice, according to no less an authority than Mr. Justice Cardozo. It is greatly to be feared that the Wisconsin court in this opinion has reenforced a trend which is slowly diverting commission procedure from a path in which it might function creatively, to one in which it will serve merely as a cog in a legalistic machine.

The Merits of the Case

In the opinion of the court the questions presented by the appeal which concern the merits of the case as distinguished from procedure are those relating to "the rate-base, the fair rate of return and the income of the company." The Wisconsin Telephone case is no exception to the general rule that, where state regulatory commissions have attempted to subject the telephone industry as represented by the Bell System to comprehensive control, the cases have been long drawn out and bitterly contested. The New York Telephone case required 10 years and the Chicago Telephone case lasted 11 years before a complete adjudication was had. The investigations of fact and issues raised have resulted in records so voluminous and in contentions so complex, conflicting, and bewildering that even the intelligent layman stands aghast. In this brief article we can do no more than to select the more important of these issues and to show how they were disposed of. Perhaps we can do no better than to jump into medias res by beginning with the fundamental rate-base issue.

The Rate-Base. In its final order the commission concludes as follows:

"The Commission has given careful consideration to the values indicated by the exhaustive appraisals in evidence before it and has studied the differences between them. It has given consideration, also, to the book cost or investment in the property. After consideration of these data, the Commission determines and finds that the fair value of the local used and useful intrastate property, including intangibles of any nature inherent in the property, is not more than $35,000,000 as a going concern."

Before deducting for accrued depreciation, the appraisals and investment in exchange plant and equipment referred to above which are the starting points for the commission finding are as follows:

Book cost, Dec. 31, 1934	$57,333,678
Hill's (staff) cost of reproduction appraisal, Dec. 31, 1934	49,256,212*
Crowell's (company) cost of reproduction appraisal, April 1, 1935	60,406,346

* Excludes certain dead drop wires.

Upon review in the circuit court, the commission's finding was modified by substituting a rate-base of $51,000,000. The supreme court, although it affirmed the decree of the circuit court setting aside the final order as unreasonable and unlawful, reached its own conclusion which differed materially from both the commission and circuit court findings. We give the supreme court's final summary of its own findings below:

Hill's appraisal of reproduction cost new as adjusted by the commission.	$53,018,854
Add:	
Difference due to use of 1929 instead of 1934 prices	3,700,000
Interest not included by the commission or added to going value	1,061,036
	$57,779,890
Less:	
2% excess plant	1,155,597*
Accrued depreciation 9.79%	5,656,651*
Interstate allocation	288,899*
	$50,678,743
Plus:	
Working capital	$ 750,000
Intangibles including going value	2,103,000
Rate-base	$53,531,743

* Deductions.

It should be noted that the basic assumption of both of the reviewing courts is that replacement costs must be given preponderant weight. Although the commission made some use of investment cost, it is plain from calculations that the basic figures are derived from a reproduction cost appraisal by its own engineering witness, which the commission says comes to $32,897,000. Its final finding of value is a judgment figure, as revealed in the above quotation, in which both the adjusted investment cost and the adjusted appraisal of replacement cost appear to contribute to the final result.

The court, speaking through Justice Rosenberry, digresses to express some views with reference to valuation of public utility properties:

"When Smyth v. Ames, Supra, was decided in 1898, public utilities were subject to little if any effective regulation. In the financial structure of utility companies, especially railway companies, was to be found a large amount of so-called water. There was no systematized accounting, and it was practically impossible to discover from the records of a utility company the so-called book cost of the property. There was therefore no other practical way to ascertain its value than to consider what it would cost to reproduce it new and then depreciate that cost to the present condition of the plant being valued. Here we have a plant which has been under State supervision since 1911 and under federal supervision since 1913, has been required annually or oftener to report to regulating authorities every dollar of its earnings and expenditures and at all times it has been subject to strict supervision as well as regulation. Just why a million and a half to two million dollars should be spent in appraising a hypothetical plant that would never be rebuilt, under assumed conditions that never can exist, on the basis of price levels, which are mere estimates, by a construction force which must be hypothetical and then assume that that represents the fair value of the plant and give it controlling weight as against the book costs which are disclosed by records kept under strict government supervision, is difficult to see" (p. 161).

The Justice then referred to his own decision in *Waukesha Gas & Electric Co.* v. *Railroad Commission*[3] in which the Wisconsin court had taken the very advanced position which not only expressed dissatisfaction with replacement costs but in effect adopted what I have elsewhere called "the going concern theory of regulation." It is known that in taking this view of the rate-base problem the court was influenced by the views of Professor John R. Commons as expressed in his *Legal Foundations of Capitalism* and by a brief submitted by Fred S. Hunt as amicus curiae. Mr. Fred S. Hunt at that time was Chairman of the Public Utilities Acquisition Committee of Milwaukee, Wis., of which the writer was Executive Secretary. This

[3] 181 Wis. 281 (1923).

committee was then negotiating a service-at-cost and acquisition contract with The Milwaukee Electric Railway and Light Co., in which all issues which normally must be disposed of in a rate proceeding were being settled contractually upon the basis of investment costs and accounting controls. However, Fred S. Hunt was also one of the two commissioners signing the order in the Telephone case. The Justice did not apparently notice that the final fair value was very close to investment costs.

The court then quotes with apparent approval the dissenting opinion of Mr. Justice Brandeis in *Missouri ex rel. Southwestern Bell Tel. Co.* v. *Public Service Commission*[4] and other more recent opinions in which the vagaries of the replacement cost standard come in for criticism. Yet, once more, as in the so-called second Waukesha Gas & Electric decision[5] the court follows what it conceives to be the law of the land:

> "While we adhere to the rule laid down by the Supreme Court of the United States it is difficult to see why a valuation arrived at by guess on the basis of estimates should form the legal basis for depriving a litigant of its property, or be the justification for excessive charges to the public." (p. 162).

In the same connection the court predicted that "there is considerable evidence that it [reproduction cost] will ultimately cease to be a dominant factor in utility valuation practice in cases where other more accurate and realistic bases are available."

With the acceptance of replacement costs as the constitutional basis of fair value determinations, the court then proceeds to add $3,700,000 to replacement costs new in order to reflect higher 1934 prices of Western Electric Co. as contrasted with what was considered by the commission to be the more normal level of 1929. Using the same basic reasoning, the court added $1,061,036 for interest during construction, although the commission had already included $2,000,000 in its reproduction figures and although actual interest during construction for approximately one actual reconstruction of the property since 1921 aggregated only $523,034.

We come now to the deductions made by the court in its own findings. Great interest attaches to the procedure adopted by the court because, if these should be sustained by the United States Supreme Court on review or if they should become established in default of a review, commission procedure would have to be significantly modified.

The first of these relates to deductions for property not considered used and useful. The commission had found that, based upon an inspection of the property, almost 8% of the same was deductible because, as a result of the depression or other causes, this amount would not be required within a reasonable time in the future. The court applied the standard that all property once prudently acquired or installed must be included. The lower court, following the company's testimony, had deducted only $117,972, whereas the commission found $4,241,508 so deductible. The supreme court, apparently without other basis than their own opinion, found that non-used or non-useful exchange plant did not exceed 2% or $1,155,597.

The most significant difference, however, resides in the amount considered deductible for accrued depreciation where depreciation expense is being provided for on a straight-line basis. This is in the opinion of the present writer the most important issue raised in this case. The commission's finding was that $12,859,279 or 28.47% was deductible.

[4] 262 U. S. 276 (1923).

[5] 191 Wis. 565 (1927).

This was based upon the actual experience of the company, a study of service lives, actual rates of depreciation applied by the company, and the accumulation of depreciation reserves under such policies. The court below had taken, as its measure of accrued depreciation, the company's evidence as to "observed depreciation" of 9.79% which, it seems, did not give adequate effect to the factor of obsolescence. The supreme court adopted the finding of 9.79% or $5,656,651.

Again it is important to note that the court did this upon the authority of what it considered to be the law of the land as derived from decisions of the United States Supreme Court. It mentioned with apparent approval the cases relied upon below, especially *McCardle* v. *Indianapolis Water Co.*,[6] and *West* v. *Chesapeake & Potomac Telephone Co.*[7] It distinguished *Lindheimer* v. *Illinois Bell Telephone Co.*,[8] relied upon by the commission. This appears from the conclusion:

"We adopt the decisions of the Supreme Court of the United States, because while confiscation is not the issue here, the result here is subject to review by the Supreme Court of the United States if it be alleged that it is confiscatory. In the Lindheimer case, the Court was not dealing with accrued depreciation, but the depreciation reserve account. It found the amount in that account so large that it would not say the rate established was confiscatory" (p. 155).

The sole remaining item concerning which a material difference exists between the findings of the commission and the court on the rate-base issue is the allowance in the rate-base for intangibles including going value. The commission's position is stated in the following:

"We have valued the property of the Company after giving consideration to the fact that the Company is a going concern and to book investment and values which include costs of training the organization of the Company and of developing routines, practices, and records to the extent that such items enter into the cost of telephone plant. We believe this gives full consideration to the element of going value and that no separate additional allowance is warranted by the facts."

The tabulation given above shows that the supreme court added $2,103,000 for intangibles including going value, even though the opinion affords no direct explanation for inclusion of this amount. Justice Rosenberry does refer to the Waukesha opinion in which, while abjuring "any attempt to deduce a formula," going concern value is set forth as one of the factors to be considered "in determining present fair value."

The Rate of Return. As previously stated, the commission had fixed a fair value for rate-base purposes of $35,000,000. In fixing upon a reasonable rate of return the commission relied upon what it called "the classic judicial statement" in *Bluefield Water Works* v. *Public Service Commission*.[9] There the Court defined such a return as "equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties." After calling attention to the fact that our Highest Court had also said that the problem was one "to be tested primarily by present day business conditions," the commission concluded that the fair return was a flexible concept, not a static, unchanging rule. In passing judgment, it took into account the financial structure, cost of capital, rate policies, efficiency and economy of management, and quality of service rendered.

[6] 272 U. S. 400 (1926).
[7] 295 U.S. 662 (1935).
[8] 282 U.S. 131 (1934).
[9] 262 U.S. 679 (1923).

The company's position, as given by legal counsel, was that a reasonable as distinct from a non-confiscatory return was something in excess of 6%, the legal maximum rate of interest. The margin above 6%, the company contended, should not be reduced merely because present costs of money were depressed because of lack of opportunity for new capital investments. Since it would not be permitted to earn as much as industrial organizations in times of prosperity, rates should not be cut to the level of industrial returns in depressions. Returns for public utilities should be regularized and not adjusted to periods of "feast and famine."

Since the commission found that the cost of capital had been hovering about 3½% and that the trend was downward, while the cost of American Telephone & Telegraph Co. funds held on call for its subsidiaries had risen from 6.42% in 1931 to 6.68% in 1934, the conclusion is announced that the historical costs of capital are not entitled to much weight in determining a reasonable present-day rate of return, "because they are inflated far above current market rates." In this connection the company's financial policy and capital structure are criticized as "evidently for the benefit of the parent company," as resulting in high capital costs "not justified by the risks and development of the business." The American Telephone and Telegraph Co.'s fixed common dividend of $9.00 per share is characterized as "not a necessary cost of attracting capital at present." The commission recalculates the present reasonable, hypothetical overall return necessary to attract capital in the present market as ranging from 4½% to 5¾%. The issue raised seems to be compressed in this statement: "Where a utility claims present-day costs of property, it is illogical to claim historical costs of capital." The commission terminates this part of its opinion with the finding "that, under present conditions, 5½% on the reasonable rate base found above is a fair and reasonable return."

The trial court had nothing to say concerning the above. It contented itself with a finding that, if the telephone rates prescribed in the final order had been in effect during 1935 and 1936, the rate of return would have been 3.6% and 3.9%, respectively.

The supreme court, likewise, did not undertake to review this feature of the commission's opinion. It was satisfied to point out that the net income as adjusted by the commission for the years from 1934 to 1938 would not yield a return in excess of 6% upon the base found reasonable by the court, which constituted no ground for saying that the existing rates were unreasonable. Even the discovery of a substantial error in the opinion of the court did not, on rehearing, change this finding.

The Net Income. This brings us to the final matter to be considered in this review, the method adopted by the commission for deriving the net income available for return. Almost half of the lengthy opinion is devoted to a review of revenues and expenses and to the development of certain adjustments in expenses designed to afford a reasonable level for fixing rates applicable for the future. Any one at all familiar with commission practices recognized that this is an important step in the process of rate regulation. In fact, controversies over the rate-base have served, as is now well known, to obscure certain questions regarding operating costs whose disposition has, from a financial point of view, been of equal pecuniary importance.

Here the commission takes up maintenance expenses, depreciation expenses, relief department and pension expense,

rate-case expenses, license fees, taxes, toll allocation, interstate segregation, and all the minutiae of telephone operating costs which are as important, if the work of regulation is to be well done, as the more strategic items of cost. It is a matter of regret that the supreme court did not see fit to pass upon these facts in some detail as did the trial court. At the close of its opinion, the court says:

"We shall not consider the so-called adjustments made in the expenses of the utility in order to establish net income. However, our failure to deal with these matters must not be construed as approval of the methods employed. In a general way, here as in consideration of the factors relating to the rate base, minimum figures are employed. No consideration is given to the fairness or justness of expenses actually incurred and made by the management; the expense account is cut down on the basis of a remanagement of the business. Where the management has not been extravagant, imprudent or wasteful, it is considered that the Commission may not ignore actual expenses because in the light of experience and present conditions, it is possible to say that some part of the expense might have been avoided" (p. 167).

Conclusion

The present writer can only register his disappointment that the Supreme Court of Wisconsin seemed to be more interested in telling an administrative agency, whose practices the court apparently did not like, that it was "off the reservation," than in taking what that commission had actually done and judging it from the point of view of constitutional tests of confiscation. Almost half of the opinion was devoted to the relatively unimportant matter of procedure, affecting, in fact, only the temporary order of 1934. The court effectively sidesteps consideration of the important issues, particularly those arising out of valuation and depreciation theory, by finding that unless it supports the lower court in reversing the commission, it would lay itself open to the charge of confiscation on the part of the Wisconsin Telephone Company under the decisions of the United States Supreme Court. It is to be hoped that this judicial piece of legerdemain will afford a basis for securing judicial review by our Highest Court.

Converted Residences and the Supply of Housing

By SCOTT KEYES*

THE failure of the construction industry to fill anywhere near the demand for housing in this country in the past decade has been the subject of much discussion. The causes of this situation have been explored, and there has been some speculation as to the potential market in view of what is assumed to be an "accumulated deficiency" arising out of the lack of new building. Although it has been recognized that a more intensive use of existing residential facilities has been necessary to accommodate families not otherwise taken care of, the adjustments that have been made are generally assumed to be temporary or "short-run" adjustments, which will be replaced later by more permanent or "long-run" adjustments. And, in the absence of quantitative data, residential conversion has been regarded as at best a negligible factor in the supply of housing.

An examination of the facts of the case, however, raises the question whether conversion has not been a more important source of housing supply in recent years than we think. A related and important question is whether conversion is really a temporary factor in the market, or whether it is in part a permanent factor.

A study of this problem in the city of Madison, Wisconsin, has yielded many pointed conclusions. In that city, conversion of existing structures has taken care of more than 1/2 of the net increase in number of families in the past decade. The dwelling units so provided comprise a large proportion of the supply of housing in the low-rent brackets. Nevertheless, the conversions have been done with relatively small investments, and a comparison of the investments with prevailing rents for this type of unit suggests the inference that they may yield relatively high returns, certainly more than could be obtained from new housing built for the same market. These conversions have been subject to little control by the city, and no allowance is made for them in any estimates of the annual increase in dwelling units. Nevertheless, two out of three of them constitute permanent additions to the supply of housing, and as such will offer serious competition to any private efforts to provide new low-cost housing, as well as inspire opposition to any public efforts to provide subsidized low-rent housing.

In 1930 Madison had a population of 57,899, composing some 15,053 families.[1] By early 1939 the population had increased to 65,319, and the number of families to 19,225,[2] so that the increase in families totaled 4,172. About 150 of these families came into the city by annexations, and presumably were already housed, leaving a total of 4,022 families to be accommodated. Yet during the same period, only 1,440 new dwelling units were provided by new construction (Table I). Thus approximately 2,582 new families in the city were not taken care of by new building.[3]

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[1] U. S. Census of 1930.

[2] "Housing Conditions in Madison: A Summary," Madison Housing Authority, Madison, Wisconsin, 1939. This figure is not strictly comparable with the census data, because hotel and institutional population is not included. Nevertheless, the number of families should be comparable in each case.

[3] In Madison, as elsewhere, there has been in recent years a growth of building in areas immediately surrounding the city. If building construction and population increase in the entire urban area were included, the proportions would change, but even so, the essential argument would remain the same.

TABLE I. NUMBER OF NEW FAMILY DWELLING UNITS CONSTRUCTED, BY TYPE OF STRUCTURE AND BY YEARS, MADISON, WISCONSIN, 1930–1939*

Year	Total	Single-Family Residence	Double or Duplex	Three-Family Residence	Apartment	Commercial Combination	Miscellaneous
Total	1,440	—	—	—	—	—	—
1930	191	125	20	12	30	3	1
1931	146	107	10	—	27	2	—
1932	74	63	4	—	7	—	—
1933	23	22	—	—	—	1	—
1934	37	31	2	—	—	4	—
1935	141	113	16	3	7	2	—
1936	232	191	32	—	6	2	1
1937	282	133	36	—	108	5	—
1938	193	—	—	—	—	—	—
1939	121†	—	—	—	—	—	—

* Data for 1930–1937 from records of the Department of Buildings, Madison, Wisconsin; for 1938–1939, from monthly reports on building construction, Bureau of Labor Statistics, U.S. Department of Labor, Washington, D.C.
† First six months only.

How were these surplus families housed? No excessive carry-over of surplus units from previous years was available for them. A vacancy survey made by the Madison Real Estate Board in October, 1930 revealed only 426 vacant dwelling units, indicating a vacancy ratio of 2.7%. Although the shortage was even more acute in 1939, some vacant units were still available. The Madison Housing Survey, a real property inventory conducted by the Madison Housing Authority in the spring of 1939, showed 367 dwelling units vacant. Yet the Survey revealed only 455 "extra families," i.e., families sharing a dwelling unit with one or more other families, which is not an unduly high figure. The answer is, obviously, that residential conversion supplied the necessary units.

According to the housing survey, 959 residential structures were converted into additional dwelling units during the years 1930 to 1939 (Table II). Data are not available at the moment to show the number of dwelling units created in these structures, but if the average number of units added in all converted structures is assumed to be about 2 (specifically, the average for all structures is 1.7), then approximately 2,000 units were created by conversion. The figures on surplus families and converted units—2,582 and 2,000, respectively—still leave many families unaccounted for, but they do indicate clearly the extent to which conversion served to plug the gap between new building and the net increase in population during the past decade.

The difficulty of making any statistical estimates of the amount of such conversion currently taking place is twofold. Almost the sole source of information on conversion is building permit records. Yet, building permit records show only a portion of the conversions.

TABLE II. NUMBER OF RESIDENTIAL STRUCTURES COMPLETELY CONVERTED, AND NUMBER PARTIALLY CONVERTED, BY YEARS, MADISON, WISCONSIN*

Year	Total	Completely Converted	Partially Converted
Total	1,632	1,029	603
No report on year	17	11	6
1935–39	539	319	220
1930–34	420	256	164
1925–29	288	197	91
1920–24	187	119	68
1915–19	90	68	22
1905–14	67	48	19
1895–1904	24	11	13
1894 or before	—	—	—

* Data from Madison Housing Survey, Madison Housing Authority, Madison, Wisconsin.

Apparently, a majority of the converters do not go through the formality of taking out a permit. In the second place, of those who do, as often as not they either fail to give complete or correct information, or the building commissioner fails to note all the information down on his records or to make a final inspection to see whether the work done conforms to the specifications.

These facts are brought out when the results of a detailed study of the records of the Madison Department of Buildings, made by the author in the spring and summer of 1938, are compared with the results of the Madison Housing Survey made the following year. In the course of the building permit study all permits issued during the years 1930 through 1937 were transcribed. Then a field recheck was made of all permits involving repairs, alterations, or additions where it appeared, either from the nature of the work or the estimated cost, that a conversion might have been contemplated. From the fragmentary evidence it was possible to piece together what seemed to be the story at that time —namely, that some 287 structures had been coverted, adding approximately 500 dwelling units to the aggregate supply of housing (Table III). It will be seen that these statistics, which would have been even smaller had it not been for the field recheck, gave evidence on only about 1/4 of the supply of units being added annually from this source.

The cost of conversions, as shown by these permits, gives some idea of the relatively low investment necessary to produce them in proportion to the rents they bring. Building permit estimates of cost are admittedly rough approximations, often biased, and the figures are offered here with full recognition of their deficiencies. The average estimated cost per dwelling unit for the entire eight-year period was about $600 (Table III). In the early years, the conversions were apparently more substantial, with the average cost reaching its peak of $880 in 1930. In 1932 the average dropped and hit a low point of only $270 per unit in 1933. Costs increased in 1934 and since 1935 the average has remained relatively stable around $650. Compared with the cost of new dwelling units shown by the same records, a converted unit was estimated to cost a little less than 1/4 of what a new apartment unit would cost and a little less than 1/8 of what a new detached residence would cost.

TABLE III. NUMBER OF BUILDING PERMITS INVOLVING CONVERSION, NUMBER OF ADDITIONAL DWELLING UNITS CREATED, AND AVERAGE ESTIMATED COST PER DWELLING UNIT, MADISON, WISCONSIN, 1930–1937*

Year	Number of Permits	Number of Units Added	Average Estimated Cost
Total	287	500	$606
1930	22	25	880
1931	29	51	719
1932	20	29	488
1933	20	27	270
1934	26	49	341
1935	63	117	629
1936	49	91	673
1937	58	111	642

* Data from records of the Department of Buildings, Madison, Wisconsin, supplemented by field recheck of all permits for additions or alterations. This recheck was made possible by assistance furnished by the Department of Agricultural Economics of the University of Wisconsin and the National Youth Administration.

The extent to which conversion has served as a source of low-rent housing in Madison is also striking. In Table IV data on monthly rents in converted units are compared with rents in non-converted units. In each of the significant low-rent brackets—$10 to $30 inclusive—units in converted structures constituted nearly 1/2 the supply, although they comprised but 23.2% of the supply in all rent brackets. In the $30 to $40 bracket, converted units made up 1/3 of the supply. This concentration of con-

verted units in the lower rental range is clearly shown on Chart I, in which all dwelling units in each rent bracket are distributed between the two categories.

TABLE IV. TOTAL DWELLING UNITS, NUMBER AND PER CENT OF UNITS IN NON-CONVERTED AND CONVERTED STRUCTURES, ACCORDING TO MONTHLY RENT, MADISON, WISCONSIN, 1939*

Monthly Rent	Total Units	Units in Non-Converted Structures	Units in Converted Structures
Total	19,137	14,691	4,446
No report	55	49	6
Less than $5.00	4	4	—
$ 5.00- 9.99	38	18	20
10.00-14.99	169	94	75
15.00-19.99	517	288	229
20.00-24.99	972	525	447
25.00-29.99	1,737	1,011	726
30.00-39.99	4,436	2,973	1,463
40.00-49.99	4,446	3,494	952
50.00-74.99	5,276	4,802	474
75.00-99.99	1,191	1,149	42
More than 99.99	296	284	12
Percentage Distribution—Type of Unit according to Monthly Rent			
Total	100.0%	100.0%	100.0%
Less than $5.00	—	—	—
$5.00- 9.99	0.2	0.1	0.4
10.00-14.99	0.9	0.7	0.6
15.00-19.99	2.7	2.0	5.0
20.00-24.99	5.1	3.6	10.5
25.00-29.99	9.1	7.0	16.4
30.00-39.99	23.2	20.1	32.9
40.00-49.99	23.3	23.8	21.4
50.00-74.99	27.6	32.8	11.6
75.00-99.99	6.2	7.9	1.0
More than 99.99	1.5	2.0	0.2
Percentage Distribution—Monthly Rent Groups according to Type of Dwelling Unit			
Total	100.0%	76.8%	23.2%
Less than $5.00	100.0	100.0	—
$5.00- 9.99	100.0	47.5	52.5
10.00-14.99	100.0	55.6	44.4
15.00-19.99	100.0	55.6	44.4
20.00-24.99	100.0	54.0	46.0
25.00-29.99	100.0	58.0	42.0
30.00-39.99	100.0	67.0	33.0
40.00-49.99	100.0	78.6	21.4
50.00-74.99	100.0	91.0	9.0
75.00-99.99	100.0	96.0	4.0
More than 99.99	100.0	96.0	4.0

* Data from Madison Housing Authority, Madison, Wisconsin.

These figures lend added weight to the general conclusion that the building industry declined during the depression years because of its inability to provide new low-cost housing.

What is more to the point for present purposes is the fact that these converted units, to the extent that they are in completely converted structures, are now a part of the permanent supply of housing, and will compete with any new low-cost housing that may be built. That is to say, the building industry will still have access to that portion of the demand arising out of a net increase in families, or out of depreciation of existing structures; but it is a moot point how much of the "accumulated deficiency" actually exists as a potential market. In Madison, of a total of 4,446 dwelling units in converted structures, 2,910 or about 2/3 have been completely converted. A "completely converted" unit is one in which the structure has been altered in such a way that difficulty would be involved in putting the structure back into its original shape.

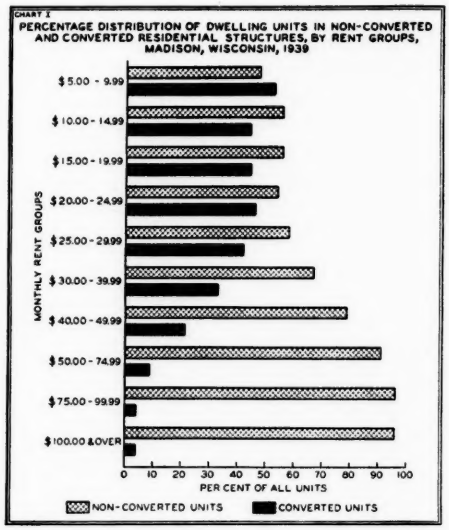

TABLE V. CONVERTED RESIDENTIAL STRUCTURES AS A PERCENTAGE OF ALL RESIDENTIAL STRUCTURES, AND DWELLING UNITS IN THESE STRUCTURES AS A PERCENTAGE OF ALL DWELLING UNITS, FOR THREE GROUPS OF CITIES, 1934–35*

Location	Structures			Dwelling Units		
	Total	Converted		Total	Converted	
		Number	Per Cent		Number	Per Cent
Total	910,478	46,986	5.2%	1,156,441	113,469	9.8%
Group III	76,690	5,030	6.6	94,724	9,465	10.0
Group IV A	107,335	6,944	6.5	124,720	15,938	12.8
Partial	—	3,585	3.4	—	8,079	6.5
Complete	—	3,359	3.1	—	7,859	6.3
Group IV B	726,453	35,012	4.8	936,997	88,066	9.4
Partial	—	15,341	2.1	—	36,571	3.9
Complete	—	19,671	2.7	—	51,495	5.5

* Data adapted from "Urban Housing: A Summary of Real Property Inventories Conducted as Work Projects, 1934-1936," Division of Social Research, Works Progress Administration, Washington, D.C., 1938. Group III contains 12 cities in W. Virginia, Pennsylvania and Wyoming; Group IV A, 13 cities in Indiana and S. Carolina; and Group IV B, 51 cities in California, Colorado, Illinois, Indiana, Kansas, Massachusetts, Minnesota, Nebraska, N. Hampshire, Ohio, Pennsylvania and Virginia.

The alterations are of a permanent nature. A "partially converted" unit, on the other hand, is one in which the alterations are of a temporary nature, and the structure can be returned to its original form without much difficulty.

Whether Madison is representative of other cities with respect to the importance of converted residential structures is an open question. But that the problem does exist to a greater or lesser extent in many other cities is indicated by data contained in numerous real property inventories conducted by the Works Progress Administration. In 76 cities in which inventories were made in 1934 and 1935, there were 113,469 dwelling units in converted structures, representing nearly 10% of the total supply of units in those cities (Table V). In 64 of the 76 cities in which a distinction was made between partial and complete conversion slightly more than 1/2 of the units were in completely converted structures.

It must be remembered that these inventories were made four and five years ago. The Madison data suggest that conversion became more important as a source of supply in the latter half of the decade, when the trek to the cities was resumed. Nevertheless, even in 1934 and 1935, conversion was an important source of supply in many cities. For example, it had provided 24.4% of the units in Martinsville, Va.; 19.5% of the units in Duluth, Minn.; and 15.7% of the units in Akron, O. The dependence of conversion on local market conditions is indicated by the extreme variation in the amount of conversion that has taken place in different cities, and makes it unwise to venture any generalizations on the basis of Madison's experience. Nevertheless, it cannot be denied that, for the country as a whole, conversion of residential structures has probably been a more important source of housing accommodations than we have been inclined to realize, and that the economic consequences of this situation are probably more permanent than we would like to believe.

Is Fair Return Appropriate for Municipal Utilities?

By RODERICK H. RILEY*

I

THE question of fair return for municipally owned utilities can, of course, arise as a practical matter only in those states in which municipal rate-making for such utilities is subject to review or approval by the state. In 3 of the 17 states where commission authority includes control of rates of municipally owned electric utilities[1] the question has recently been raised in interesting fashion.

With the reorganization of the Wisconsin commission in 1931 and the accompanying broadening of its jurisdiction and increase of its administrative and financial strength,[2] all aspects of policy were reconsidered. In the view of the first chairman of the new commission, the late Theodore Kronshage, fair return was inappropriate for municipal plants and he advocated a no-profit rate policy. This position was not shared by the other commissioners, however, and the policy was adopted of allowing, in addition to local and school tax equivalents, a fair return upon the book value less the depreciation reserve.[3] This policy, based upon the commission's interpretation of the statutes, has since been ratified by the legislature in an amendment to the law governing municipal utilities.[4]

The Indiana commission, in the Logansport case,[5] relied upon an opinion of the attorney general that "all doubts, if any exist, as to the intention of the legislature to provide for the support of municipal government by means of municipally owned utility earnings should be resolved against such intention."[6] In its decision the commission accordingly denied the municipality not only the right to earn a fair return but also the right to charge rates to cover payments in lieu of taxes. Upon a general finding that a municipality acts in its private capacity in operating a utility, the state supreme court reversed the commission on the former point, while sustaining it upon the latter.[7]

It is interesting that the Indiana court's decision turned upon a finding of private capacity. The contention that a municipal utility has full rights as a private person has also been raised in opposition to the policy of the New York commission, to which our attention will be chiefly directed.

The decision of the New York Court of Appeals in the Boonville case[8] sustained the lower courts[9] in holding the Public Service Commission to be without statutory authority to disregard the requirement of fair return in determining

* Industrial Economics Division, United States Department of Commerce.

[1] As of January, 1937. C. O. Ruggles, *Aspects of the Organization, Functions, and Financing of State Public Utility Commissions* (Boston: Harvard Graduate School of Business Administration, 1937), pp. 51–2.

[2] Wis. Laws 1931, c's 183 and 475.

[3] For a discussion of the development of Wisconsin policy since 1931 see the writer's article, "Municipal Utility Regulation in Wisconsin," 22 *Public Utilities Fortnightly* 300 (September 1, 1938).

[4] Wis. Laws 1937, c. 100.

[5] *Re Hillis* (1926), P.U.R. 1927 A 443.

[6] *Ibid.*, at 452.

[7] *Logansport v. Pub. Serv. Com.*, 177 N.E. 249 (1931).

[8] *Village of Boonville v. Maltbie et al.*, 272 N. Y. 40; 4 N.E. (2d) 209; 15 P.U.R. (N.S.) 376 (1936).

[9] 281 N. Y. Supp. 787; 9 P.U.R. (N.S.) 265 (1935); 283 N. Y. Supp. 460; 245 App. Div. 468; 14 P.U.R. (N.S.) 93 (1935).

municipal utility rates.[10] The court expressly declined to consider whether municipal utilities had the same constitutional claim to fair return as that enjoyed by private utilities.[11] That issue was left to be raised in the event the legislature should alter the present statute[12] and require or empower the Public Service Commission to eliminate profit from municipal utility operations.

Chief Judge Crane, in a concurring opinion, saw no good reason for dodging the constitutional issue:[13]

". . . As the right [to construct and maintain its own municipal electric light plant] originates with the Legislature it may limit the use and exercise of this right as it sees fit. A village is not deprived of its property, within the meaning of the Federal Constitution, when the Legislature or any of its agencies fixes the rates which municipal light plants may charge. If, therefore, the Legislature should provide that municipalities taking over the electric light business should run it at cost and that the consumers should not be charged such a rate as to give the municipality a profit over and above cost of operation, such an enactment would be legal and constitutional."

Following the decision of the Court of Appeals, the Lehman administration sought the enactment of legislation requiring municipal utilities to provide service at the lowest possible rates, thus precluding the use of utility revenues for other municipal purposes.[14] Opponents of this policy were successful in preventing passage of this legislation and carried the controversy one step farther, into the state constitutional convention of 1938. Dividing on what were recognized as economic rather than party lines, the convention by a vote of 110 to 30 adopted the Schenck proposal.[15] This provision, as a part of the "omnibus" amendment, was subsequently approved in the November 8, 1938 referendum[16] and is now incorporated in the constitution as Section 18 of Article III. In the official summary issued by the convention, it appeared as follows:[17]

"*Municipal Utility Plants.* Where municipalities operate their own utility plants, the legislature may not prohibit a fair return on the plant value or the use of such return for municipal purposes or for payment of refunds to consumers."

The issue thus raised in New York is, of course, intimately related to the general issue of utility regulation by means of public competition. The new constistitutional provision is in fact known as an "anti-yardstick" measure. The Boonville case thus acquires significance as a focal point for consideration of the economics of public operation of utilities.

The question before the court in the Boonville case was whether the Public Service Commission of New York had legal authority to require a municipal utility to forego a fair return on its property. The correlative economic question, which was raised by the commission and argued by counsel for the village, is the appropriateness of fair return in rate-making for municipal utilities. Essentially economic, this question is also legal in nature because of the judicial origin

[10] For proceedings before the commission see *Customers of Electricity v. Village of Boonville*, 5 P.U.R. (N.S.) 298 (1934); rehearing, 8 P.U.R. (N.S.) 493 (1935).

[11] 272 N. Y. 40 at 46.

[12] Sec. 364 of Art 14-A of General Muncipal Law (c. 23 of Consol. Laws of New York): "Except that a municipal corporation need not apply to or obtain from the public service commission a certificate of authority for a public utility service under this article, all of the provisions of article four [general powers of the commission, including rate-making] of the public service law, so far as the same are applicable, shall apply to a municipal corporation furnishing a public utility service under this article."

[13] 272 N. Y. 40 at 50.

[14] See message of Governor Lehman, Jan. 5, 1938, *New York Times*, Jan. 6, 1938.

[15] *New York Times*, Aug. 26, 1938.

[16] *New York Times*, Nov. 9, 1938.

[17] *New York Times*, Aug. 26, 1938.

and definition of the terms "fair return" and "fair value."

The basic position taken by the New York commission in the Boonville case is expressed in the following excerpt from its decision after rehearing:[18]

"It seems to us that the primary purpose for which municipalities are organized is to furnish service, which includes electricity in this case, to the public as economically, efficiently, and satisfactorily as possible. Its primary object is to make these modern conveniences and necessities available to its residents at as low a rate as it reasonably can. The profit motive should not enter into the consideration, and the Commission believes that it is against sound public policy to accumulate profits from the operation of municipal plants over and above all costs and suitable reserves, so that such profits may be transferred to the village funds and used to pay taxes or to promote other municipal projects. This is indirect taxation on rate-payers who are not necessarily the same persons as the taxpayers, or where identical, who do not pay electric bills in the same proportion that they pay tax bills."

The Village of Boonville, together with other members of the Municipal Utilities Association (all members being New York municipalities), opposed this interpretation of the nature and status of municipal utilities, and insisted upon the proprietary and private nature of the function performed by a municipality in operating a utility. Acting in its proprietary capacity, it was argued, the village has full private rights, including the constitutional right to a fair return on the fair value of its used and useful utility property. The heart of this argument is contained in the following excerpt from the association's brief in the first proceedings before the commission:[19]

"(c) *To make a municipality run its electric plant at cost would be robbing the tax-payers to benefit the consumers of electricity. There is no excuse in economics, in common sense, or in decency for extorting higher taxes from the tax-payers in order to give consumers of electricity lower rates.* [Italics in the original.]

"Since the municipality may lawfully make and sell electricity and in so doing acts in its private or proprietary capacity, the taxpayers whose money has been used or credit pledged and debt limit *pro tanto* absorbed to build the electric plant, are in fairness and common sense in precisely the position of the stockholders of a utility corporation. Practically, though not technically, they own the plant. It was built for the benefit of the corporation, (whether municipally or privately owned). In the case of a city or village, it could not, under the constitution, have lawfully been built for the benefit of the consumers of current.

"Every privately owned utility, of course is safe from confiscation of its property by the state, and under the cases heretofore discussed, municipally owned utilities operated as they are in a private or proprietary capacity, are likewise safe from such confiscation.

"Every privately owned utility is entitled as a matter of course not only to rates which will reimburse its cost of operation, but to rates which will produce a fair return on its property used and convenient for the public service."

In answering this argument, the commission said:[20]

"The courts have held that a municipality which supplies public utility service to its inhabitants generally (and not for purely municipal purposes) is acting in its proprietary capacity and not in its governmental capacity. [Citations omitted.]

"But Mr. Andrews [of counsel for the association] jumps from 'proprietary' to 'private' without pausing to consider whether there is a difference or attempting to establish that they are one and the same thing. Then he takes a further leap by assuming without authority that if a municipality is operating a public utility in a 'private' capacity, it has the 'right' to charge rates in excess of cost because the courts under constitutional provisions for the protection of *private* property have laid down certain rules to be followed by regulatory bodies in dealing with private corporations."

[18] 8 P.U.R. (N.S.) 493 at 498.

[19] New York State Public Service Commission, Case 7593, Brief filed by Municipal Electric Utilities Association, Point II, Subsection (c).

[20] 5 P.U.R. (N.S.) 298 at 310 (1934).

The commission did not attempt to analyze the difference between proprietary and private functions of a municipality, nor did it pursue further inquiry into the nature of property entitled to constitutional protection. To refute the association's general position, however, the commission quoted from the decision in *Niagara, Lockport & Ontario Co.* v. *Prendergast*,[21] which had been cited by the association. The commission agreed with the association that the question at issue in that case was

"what elements the city could be compelled to include in its rates in order to comply with the charter provisions requiring it to operate at not less than cost at the place of delivery, [whereas] our question is, of course, what elements the city or village can be compelled to forego by authority of the state or Public Service Commission—what elements, conversely, constitute a part of its legal rights, its property, which cannot be confiscated."[22]

The commission proceeded, however, to point out that "the opinion of the court in spirit and tenor indicates that a municipality ought not to charge rates returning a profit over and above the elements of cost therein provided for,"[23] and quoted at length from the majority opinion in that case:

"While we do not purport to list all the items which the Commission should consider in ascertaining cost, yet the following discussion seems to be required. The rules laid down as to a return upon a capital invested in privately owned plants do not apply. Compensation and profit are paid to a private investor who embarks his capital in a utility venture. He is entitled to a fair return upon the reasonable value of the property used. [Citations omitted.] The character of the city of Jamestown does not require that a price be fixed which will return a profit. Gain upon the capital invested is a profit. [Citation omitted.] If the plant has been paid for from the profits of its operation, no return upon its value is required. If general city funds have been used in the construction of the plant, the city should receive a return thereon at least at the rate it would have paid on a loan of like amount."[24]

II

The claim that a given activity or function of a municipality is an exercise of its proprietary or private capacity arises generally either to support an action to enforce the municipality's liability for a tort or to protect the municipality against interference by the legislature.

Although the terms "proprietary" and "private" are used interchangeably by the courts, it appears that the former is more appropriate to determinations of liability, the latter to determinations of freedom from state interference. The most significant single circumstance in determining proprietary capacity in liability cases appears to be whether the activity be conducted for profit.[25] On the other hand, in determining the limits to legislative interference, the courts seek to discover whether the function is one serving only the locality or is properly to be regarded as serving citizens of the state who are only incidentally municipal citizens as well.[26] In the former case, the function may be considered an exercise of the municipality's private powers.

Because a municipal corporation's powers are dual, not triune, it is apparent that those which are not governmental must be corporate. To argue from this that proprietary and private functions, both being non-governmental, are therefore identical is, however, to

[21] 229 App. Div. 295; 241 N. Y. Supp. 162; P.U.R. 1930 D 58 (1930).

[22] 5 P.U.R. (N.S.) 298 at 304 (1934) but already cited in n. 10 above.

[23] *Ibid.*, at 304.

[24] P.U.R. 1930 D 58 at 63 (1930); quoted in 5 P.U.R. (N.S.) 298 at 304–5 (1934).

[25] 6 (rev.) McQuillin on Municipal Corporations, 2d ed., §2845 (2673).

[26] 1 McQuillin, *op. cit.*, 2d ed., §190 (169); 1 Dillon on Municipal Corporations, 5th ed., §116; *Mt. Hope Cemetery v. Boston*, 158 Mass. 509; 33 N.E. 695 (1893).

overlook the fact that powers are defined only in given legal contexts.[27] It is not unusual for apparently conflicting findings to be made upon the same facts by the same court, where the legal issue is different in the several causes. And a finding in one need not render another *res judicata*. In defining municipal powers, the courts are faced now with a tort action, now with an action to restrain the legislature or its agents. Consequently it appears quite possible for a municipal activity to be held governmental, and hence carrying immunity from suit, and in another cause to be found private and hence free from legislative interference. Further to complicate the situation are rulings to the general effect that even recognizedly private functions of the municipality are subject to legislative control,[28] one court going so far as to say that

"it is thoroughly established that the plenary authority of the legislature to restrict and limit the exercise of municipal powers extends to all municipal powers granted by it, whether public or government, proprietary, or private."[29]

Decisions of the United States Supreme Court indicate that the Federal Constitution contains no hindrance to a state in adopting a policy of state operation of utilities.[30] Whether a state could, by a declaration of policy, in effect convert existing municipally owned utilities into state utilities merely administered by the municipalities under state-made rules is not entirely clear from these decisions. In a recent case, the Court has expressed a view that in operating a utility "the municipality is exercising a part of the sovereign power of the state."[31] This would seem to indicate implicit state power to limit and regulate such utilities in accordance with any state policy determined upon. If so, it is idle to speculate whether such functions are governmental or corporate in nature, since the issue of state control would be settled by the broader ruling.

Despite the confusion which prevails in this field of the law and which is noted at length in the authorities,[32] the following statements may be ventured:

(1) A municipality ordinarily acts in its proprietary capacity in operating a utility. Apparently it is within the power of the legislature, if not specifically restrained by the state constitution, to make such operation a governmental function.

(2) Determinations of proprietary capacity relate to a municipality's liability for torts and also establish rights against other persons. A finding of proprietary capacity does not require that the municipality's rights against interference by the legislature be the same as those of private persons, and in some jurisdictions no limit is recognized to the legislature's control of municipalities in their corporate capacity.

The further question, whether, if a municipality be held to have rights under regulation on the same basis as private utilities, the right to a fair return has the same meaning and substantive content as for private utilities, requires further analysis.

[27] Cf. 3 Dillon, *op. cit.*, 5th ed., §1303.

[28] *Darlington v. N. Y.*, 31 N. Y. 164 (1865); *David v. Portland Water Committee*, 14 Ore. 98; 12 Pac. 174 (1886).

[29] *Twohy Bros. Co. v. Ochhoco Irrig. Dist.*, 108 Ore. 1; 216 Pac. 189 (1923).

[30] *Green v. Frazier*, 253 U. S. 233 (1920); *Jones v. Portland*, 245 U. S. 217 (1917), cited by the Court in *Puget Sound Power & Light Co. v. Seattle*, 291 U. S. 619 at 624 (1934). But note that in the Puget Sound opinion the Court speaks of a state "engaging, *in the public interest*, in enterprises" (italics supplied); also that in *Jones v. Portland* great stress was laid upon the non-profit character of the operation of a municipal fuel yard.

[31] *Puget Sound Power & Light Co. v. Seattle*, *supra* n. 39 at 624.

[32] 1 McQuillin, *op. cit.*, 2nd ed., §191 (170); 1 Dillon, *op. cit.*, 5th ed., §116.

III

The economic appropriateness of fair return in municipal utility rate-making may be examined from two angles: the economic necessity of fair return, and the compatability of fair return with the economic policy appropriate to public operation.

The fair return doctrine of the Supreme Court rests upon the definition of property adopted by the Court majority in the first Minnesota Rate Case.[33] Previous decisions interpreting the Fourteenth Amendment[34] had employed a definition of property in the physical sense, there being no deprivation in the absence of a physical taking. In the Minnesota case the essence of property was held to be the fair market value of its earning power. To use Professor Commons' terms, the Court shifted from a use-value definition to an exchange-value definition of property.[35]

The significance for our present study of the Court's definition of property as exchange value should be apparent. If this is the sole meaning of property under the Fourteenth Amendment, then to admit that a municipality has corporate property is to concede it the right to a fair return, unless the constitutional protection does not apply. Deprivation of fair return is *pro tanto* deprivation of exchange value. To support a no-profit rate policy on the part of the legislature or commission, it is necessary either to declare that all municipal property, both governmental and corporate, is held for use and not for exchange, and thus is protected only from physical confiscation, or to declare that legislative control of municipalities is not limited by the Fourteenth Amendment. In the Boonville case, the commission—implicitly rather than explicitly—took the former position, and Chief Judge Crane would have had the court take the latter.

Building on the concept of property as value in exchange, the court has developed fair return on fair value as a minimum amount of earnings over expenses that will protect the utility corporation from being unconstitutionally deprived of its property. The economist can agree with the court that there is a return on the utility investment that must necessarily be yielded if the enterprise is to continue as a going concern. This may be termed the necessary supply price or the opportunity cost of capital. The economist may gravely doubt the court's success in developing legal rules to determine what this return is in each case, but he will agree that—under conditions of private enterprise, with the utility competing in the market for investment funds—there must be a reward offered that is sufficiently large to attract capital in competition with other investment opportunities.[36]

It clearly does not follow that the economist will necessarily hold the same view with regard to an enterprise which draws its capital funds, not from the investment market, but from municipal coffers. For the usual market determination of the flow of capital funds, municipal ownership substitutes a budgetary determination. Consequently, principles based upon the former method are not necessarily applicable—indeed are presumptively inapplicable—where the latter method is relied upon. This, it will be noted, is but the obverse of the proposition that municipal property is held for use. For in the case of a non-

[33] *C.M. & St. P. Ry. Co. v. Minnesota*, 134 U. S. 418 (1890).

[34] *The Slaughter-House Cases*, 83 U. S. (16 Wallace) 36 (1873); *Munn v. Illinois*, 94 U. S. 113 (1876).

[35] John R. Commons, *The Legal Foundations of Capitalism* (New York: Macmillan Co., 1924), p. 14.

[36] Cf. M. G. Glaeser, *Outlines of Public Utility Economics* (New York: Macmillan Co., 1927), pp. 414–28.

commercial decision as to an outlay of funds, we are dealing with a situation analogous to household economics rather than business economics, with use value rather than exchange value.

It may be argued that the foregoing characterization is inaccurate and that indirectly, by affecting the budgetary decision, the same financial factors operate as in the private field. Clearly, however, the consideration of financial reward is not dominant, as under private enterprise it must be. The prospect of tax reduction may be included, but it is not of the essence. Municipal ownership has often resulted from dissatisfaction with rates under private ownership. It will be generally conceded that in such a case the citizens were anxious to eliminate unnecessary charges. It can hardly be said that they must have intended to retain the charge of fair return, which through their action also became unnecessary. Further, if in any given instance such a purely financial basis of municipal action were found, it would remain to be shown that in authorizing municipal ownership the state legislature or constitutional convention had intended that financial considerations should take precedence over the full discharge of a public function. (This intent, of course, is apparent in the 1938 constitution of New York.)

In recognizing the public character of the function performed by a municipal utility we approach the heart of our problem. It will be useful to recall the rule enunciated in *Olcott* v. *The Supervisors* and recently reiterated in a modern setting: "No matter who is the agent, the function performed is that of the state."[37] The legal rule which supports the exercise of the power of eminent domain by or in behalf of utilities and railroads and which authorizes the state to raise funds by taxation or borrowing for utility or railroad purposes is based upon recognition of the public function that these enterprises discharge. As was stated in *Olcott* v. *The Supervisors*:[38]

> "A railroad, although constructed and owned by a private corporation, is for a public use, and the right of eminent domain of the state may be exerted to facilitate its construction, and taxes may be imposed by the state in furtherance of that use."

The methods by which public functions are financed are in general three: by taxation, by administrative charges, and by prices. The selection of the method or the combination of methods of financing any given function should depend upon the public policy at issue.[39] Highways have been financed by toll charges, by taxation, and by administrative revenues. Certain other public services are typically financed out of one or another of these types of revenue. The leading case just cited is typical of a combination of price revenues (raised by the private corporation) and tax revenues (raised by the state), which was deemed appropriate in building up the railroads. No ironclad rule determines which method shall be employed in any given case. In some cases only one method is feasible; in many instances resort to any basis but that of general taxation would seriously affect the adequacy of performance of the public function.

A major consideration, where a price charge is contemplated, must of course be the effect of price in restricting demand. Where widespread effective demand is in the public interest, price reductions will be in order until a point is reached where further expansion of de-

[37] 83 U. S. (16 Wallace) 678 at 695 (1873); *Milheim v. Moffat Tunnel Dist.*, 262 U. S. 710 at 719 (1923).

[38] 83 U. S. (16 Wallace) 678 at 695.

[39] Cf. John Bauer, "Rates and Revenues of Public Enterprises," 183 *Annals of the American Academy* 70 (January, 1936).

mand involves substantial wastage of the service. Should this point be so low that the service requires supplementation of price revenue by taxation, the determination to be made will be similar to that in other matters concerning public expenditures and will involve balancing the additional taxation against the additional social advantage of extending the use of the service.

So long as a municipal utility is treated as of purely or predominantly local importance, it is difficult to argue that the method of financing should not be left to the municipal authorities. It may be deemed best to treat the utility as a strictly business venture of the municipality and to set rates entirely on the basis of what the traffic will bear, i.e., as an unregulated monopolist would set rates. This, of course, permits a portion of municipal revenues—and in some instances a major portion—to be derived from what is in effect a sales tax on electricity. The regressive character of such a tax[40] persists even when the municipality's profit is modest, whether through restraint or otherwise. (Query: Does fair return, to the extent it exceeds actual capital costs, constitute such a tax?) There have been municipal water utilities operated under the extreme contrary principle—namely, no charge to the consumer. In any municipality the determination to subsidize any utility completely could conceivably be made. And unless the state is admitted to have a superior interest, the determination is entirely for the municipality to make.

As to the extension of the state's power over a local utility, if the problem arises in a jurisdiction where the state's authority over the corporate functions of the municipality is held to be plenary, intervention by the legislature is of course its own justification. Where the distinction is made between functions of predominantly or purely local significance and those which are of state-wide concern, a broader declaration of state policy than that implicit in an isolated act of intervention would probably be necessary. It seems to the present writer to be beyond question that inclusion of municipal plants within the definition of public utilities subject to commission regulation constitutes such a declaration of policy and establishes the superior interest of the state over that of the municipality. It follows, therefore, that in states where the commission exercises jurisdiction over the rates of municipal utilities, the entire rate policy of such utilities should be based upon considerations of state-wide public policy rather than local only.

Another contention is raised to strengthen the argument for fair return, which would balk the application of state policy. It is argued that, so long as the rates of a municipal utility do not exceed those of comparable neighboring private utilities under state regulation, the municipal rates must be deemed reasonable. In other words, until the state finds private rates unreasonably high and effectively requires a reduction, it should refrain or should be barred from requiring a downward revision of municipal rates which, under like conditions, are no higher. This view is found in the association's brief in the Boonville case:[41]

"A final reason why this Commission should be unwilling to order all municipally owned utilities to operate at cost is found in a comparison of the average rates they charge for domestic use of electricity, to the similar average rates charged by privately owned utilities, in communities of comparative size. The average domestic rates in cities and villages owning their own electric plants are substantially lower than those in similar

[40] For an analysis of the tax characteristics of a specific case of municipal utility charges, see Howard K. Hyde, "Municipal Utility Profits or Taxes?" 12 *Journal of Land & Public Utility Economics* 212 (May, 1936).

[41] See n. 19 *supra*.

communities served by private power companies. It is difficult, therefore, to see how these lower rates could conceivably be called improper, unreasonable or discriminatory."

Three contentions seem to underlie this view: (1) State regulation of private utilities is satisfactorily effective and prevailing private rates are therefore reasonable, without regard to the administrative and financial competence of the state commission or to the legal difficulties which it may have encountered in seeking rate revision. (2) Alternatively, if state regulation is defective, the people of the state nevertheless have no valid claim to such benefits as a state policy of public competition would add to those of usual regulatory processes. (3) Most significant is the implication that the appropriate standard in an admittedly public industry is that of private business.

Private enterprise engaged in furnishing utility services derives certain unquestioned advantages from the principle that "no matter who is the agent, the function is that of the state." But although the agent be public, so the implied contention runs, the pricing policy must nevertheless be that which is necessary when the state's function is discharged by private enterprise. It is a strange rule that forbids a state to require that a municipality, in discharging a public function, shall apply principles of public economics; and that insists on the right of the municipality, although the function is unquestionably public, to apply a standard which is appropriate only to private business economics. This strange rule, however, is now embedded in the state constitution of New York.[42]

Despite the declaration of the Court of Appeals in the Boonville decision that it would give no consideration to the constitutional issue, it should be apparent from the foregoing analysis that its decision necessarily implies that municipal property has the same meaning as the Supreme Court has given private property under the Fourteenth Amendment. Only the applicability of the protection of the Fourteenth Amendment was not decided; the applicability of its terms was tacitly conceded.

This conclusion follows from the court's reliance upon the wording of Section 364 of the General Municipal Law, which makes municipal utilities subject to the provisions of the Public Service Law, "so far as the same are applicable."[43] As we have seen, the applicability of the doctrine of fair return depends upon the definition of property as exchange value. If property be defined as use value, lack of fair return involves no deprivation of property, and the issue may be dismissed.

Chief Judge Crane, who wished the court to affirm the right of the legislature to control municipal functions, i.e., to find that the protection of the Fourteenth Amendment does not extend to municipalities, also relied upon the provisions of Section 364 to support his concurrence in the majority decision.

It is apparent in these proceedings, as elsewhere, that even proponents of municipal ownership of utilities commonly misunderstand the nature of public economics and insist upon applying private business standards without regard to their appropriateness. We may therefore readily concede that the legislature never intended that municipal utilities be treated on a different basis than private utilities. But the commission did not pose the issue so as to require the courts to determine what the intention of the legislature must have been. Had it done so, it probably could have forced them to rest the adverse decision upon recognition of the legislature's misapprehension of the principles of public economics.

[42] This rule also prevails, of course, in Indiana under the Logansport decision (*supra*, n. 7) and in Wisconsin under statutory confirmation of commission policy (*supra*, n. 4).

[43] See n. 12, *supra*.

II. Legal Possibilities and Limitations of Milk Distribution as a Public Utility*

By W. P. MORTENSON†

THE previous installment of this article contained a discussion of the legislative acts dealing with milk price regulation and the litigation over their legality, which involved the power of the state or Federal Government to fix prices under competitive conditions. None of the cases there discussed involved the question of a legislative monopoly. So far as the writer knows, no state legislative acts have been passed and put into operation to make milk a public utility in the ordinary meaning of the term.

If, however, milk distribution were to be declared by law to be a public utility, methods of operating the business would be materially changed. One company, or at most two or three companies, would supply all the milk in a given market area or areas; delivery service would be coordinated; handling of accounts would be centralized; and regulation, instead of applying only to sanitation and quality of the product, would be extended to prices charged consumers as well as prices paid to farmers, to the profits of the company, to the time of delivery and quality of service generally, and to various other aspects of the business.

If those who assume responsibility for its operations have the will and the capacity to operate it efficiently, such a system of distribution will undoubtedly make for lower costs of handling and hence permit lower milk prices to the consumer. Accordingly, the system may, and can, be the basis for promoting the public welfare because (1) dietitians are in general agreement that milk is a health building food and a virtual necessity for infants and growing children, and (2) many of the lower income families are not consuming the desired amounts of milk, partly because of the inadequacy of the family budget to provide the more common food necessities including milk. It would require no undue strain on the imagination to see that an increase in nutritional standards, made possible by lower prices of an important or essential food product, would contribute to the health and vigor of the race.

But, though the dietitian and even the layman may agree that milk is sufficiently important that in their judgment its distribution is "clothed with a public interest" and therefore may properly be declared a public utility by the legislature, the question still remains, "Will the courts agree?"

On the assumption that in the future the United States Supreme Court does not reverse the position held in the cases cited in the previous article, will those cases serve as a basis to set at rest the question of whether the business of processing and distributing milk may be operated as a public utility under an

* For Part I of this article see 15 *Journal of Land & Public Utility Economics* 438–47 (November, 1939). Footnotes are numbered consecutively with those in the first installment.

Note. Two errors have been discovered in this first installment. On p. 441, column 2, line 2, the year should have been "1933" rather than "1935," and on p. 447, column 2, the first sentence in the quotation should have read: "The authority of the Federal government over interstate commerce does not differ in extent or character from that retained by the states over intrastate [not "interstate," as printed] commerce. . . ."

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exclusive license or franchise? Since the legality of a controlled monopoly was not at issue, we will need to go beyond these cases for the necessary information. A brief historical outline of regulation as it has manifested itself primarily in the field of the more typical public utilities will aid in attempting to foretell the position that courts may take.[30]

Unification an Extension of an Established Trend

The American public seems always to have had confidence that the force of competition would bring about a supply of commodities and services at reasonable prices and rates. It has apparently assumed that the "natural law of supply and demand" could be depended upon to protect the public welfare. Formerly this faith in competition existed not only in the case of those businesses which were distinctly private in their nature and which were operated as small business units, but until about the beginning of the present century it appeared as well in the operation of those businesses which have since been set up and operated as regulated monopolies—public utilities under legislative grants.

For example, for a considerable period of years after electric light and the gas used for heating and lighting purposes were in common use, the public continued to foster competition among several companies operating in one city. In 1887, for instance, New York City granted franchises to six electric light companies. Indeed, the granting of franchises to operate competing utility companies was a common practice everywhere. Competition in this latter group of businesses with its duplication of capital and effort proved, however, to be wasteful and expensive. If competitive forces did eliminate all but the most efficient company—or the one which for other reasons was able to outlive the rest in a struggle for existence—the result was an unregulated or at best an improperly regulated monopoly. "Experience convinced nearly every community, sooner or later, that the beneficent results usually attributed to competition were not being realized."[31] The fact finally became obvious that better services could be obtained through a system of monopolies regulated by the public for the common benefit.

The Sherman Anti-Trust Act of 1890 is a clear case of the faith of the American people in the beneficent operation of competition on a national level. This Act was designed to break down certain monopolies which had developed because of the economic and social conditions favoring them. They were usually the result of a combination of several competing businesses into one giant monopoly, either entirely unregulated or inadequately regulated from the public point of view. This is not to be confused with a monopoly granted by legislatures.

Prior to passage of the Sherman Act, the American Tobacco Company and the Standard Oil Company of New Jersey were almost complete monopolies. "By order of the courts, the American Tobacco Company was divided into four large competing concerns."[32] The oil company was ordered broken down

[30] Since the cases upon which we must rely are not entirely parallel to public utility control of the milk business, it will be necessary to reason almost entirely by analogy. Accordingly, care must be exercised to avoid erroneous conclusions, since there is no way of knowing the conditions under which the litigation will come before the courts or the factual materials which will be contained in the briefs and records. The courts have consistently avoided laying down a blanket test for judging whether a particular business would be classed as a private or a public calling.

[31] Eliot Jones and Truman Bigham, *Principles of Public Utilities* (New York: Macmillan Co., 1931), p. 68; see also pp. 14 and 57.

[32] Sumner H. Slichter, *Modern Economic Society* (New York: Henry Holt & Co., 1931), p. 359.

in a similar manner. Albeit Sections 1 and 2 of the Sherman Anti-Trust Act make the restraint of trade and monopoly respectively illegal, it was not intended to destroy monopolies created by legislative grants. This fact was settled in a circuit court case:

"In construing the federal and state statutes, we exclude from consideration all monopolies which exist by legislative grant; for we think the word 'monopolize' cannot be intended to be used with reference to the acquisition of exclusive rights under government concession, but that the lawmaker has used the word to mean 'to aggregate' or 'concentrate' in the hands of a few, practically and, as a matter of fact, according to the known results of human action to the exclusion of others; to accomplish this end by what, in popular language, is expressed in the word 'pooling,' which may be defined to be an aggregation of property or capital belonging to different persons, with a view to common liabilities and profits."[33]

It follows, therefore, that the distribution of milk by a company, which has gained monopoly control of a market through a normal trend of business, by forcing its competitors to the wall or by buying them out, could legally be broken down into competing units in accordance with the provisions of the Sherman Anti-Trust Act. But if that same company had been granted a monopoly through legislative action, its operation would be legally permitted under the Act[34] if, in the judgment of the court, such action was not contrary to public welfare.

Leaving out of consideration the question of municipal or city ownership of the milk distributing business, the question concerning the legality of public utility control—a controlled monopoly—will turn mainly on one of two points: (1) Will the United States Supreme Court rule that the business of processing and distributing milk is so distinctly a private competitive business—a common calling—that it cannot constitutionally be subjected to the complete public regulation generally imposed over typical public utilities? or (2) Will it hold, as it has in more recent cases, that there is no closed class or category of business "affected with a public interest"?

In a modern economy, especially as it manifests itself in the complex relationships of industry and trade, can businesses by their nature be classified into those which are strictly private and those which are sufficiently clothed with a public interest to require substantially complete social and economic regulation? Obviously, any attempt at such classification into clear-cut categories would sooner or later place courts in an extremely untenable position. In the Nebbia case the Court took the position that rigid categories of this nature cannot be so established. Such a position would seem to fit much more closely the everyday business conditions in a complex society than would the opposite point of view. Hence, there seems good reason to believe that this position may prevail in court decisions involving future issues of public regulation.

One cannot, however, be confident in his prediction because decisions sometimes emanate from the Supreme Court which are puzzling to the laity and to economists as well. In a case somewhat analogous to those which might test the validity of milk as a public utility, the United States Supreme Court did not uphold such control. In 1925 the Oklahoma legislature declared the manufacture of ice for sale and distribution to be a "public business," or public utility. Powers of regulation, similar to those

[33] *Amer. Biscuit & Mfg. Co. v. Klotz*, 44 Fed. 721 at 724 (1891).

[34] Actually the company is granted an exclusive franchise by the city or municipality. The right of granting this monopoly is conferred upon these units of government by the state.

customarily exercised over public utilities, were conferred upon the State Corporation Commission.[35] For a period of five years the act remained unchallenged and there was little competition in the ice industry in that state. One-third of the ice plants were owned and operated by public service corporations which conducted the ice business in connection with their public utility business.

Under the provisions of the act, before obtaining a license to operate, an applicant was required to show a public necessity for a new company entering into the manufacture and sale of ice in the community in which he proposed to operate. The legal procedure called for a hearing before the Corporation Commission for the purpose of receiving applications and hearing the testimony of prospective ice distributors and others concerned. If, at the close of the hearing, the Commission decided that the public needs were already being served adequately, it could deny the applicant a license.

In spite of the law, a Mr. Liebmann had engaged in the ice business without obtaining a license. A competitor, the New State Ice Company which had been engaged in manufacturing and selling ice under a license, brought suit against Liebmann for operating without the required license. Liebmann contended that the business of manufacturing ice for sale was not a public business, but instead a private business and a common calling, and the right to engage in a common calling is one of the fundamental liberties guaranteed by the due process clause. To make the right to engage in a common calling dependent upon the finding of a public necessity deprived him of liberty and property in violation of the Fourteenth Amendment.

The case reached the United States Supreme Court which declared the Oklahoma law unconstitutional and ruled that "all businesses are subject to some measure of public regulation . . . but the question here is whether the business is so charged with a public use as to justify the particular restriction above stated."[36] On the most salient point of the case the Court spoke with positiveness:

"Here we are dealing with an ordinary business, not with a paramount industry upon which the prosperity of the entire state in a large measure depends. It is a business as essentially private in its nature as the businesses of the grocer, the dairyman, the butcher, the baker, the shoemaker, or the tailor, each of whom performs a service which, to a greater or lesser extent, the community is dependent upon and is interested in having maintained; but which bears no such relation to the public as to warrant its inclusion in the category of business charged with a public use."[37]

"There is nothing in the product that we can perceive on which to rest a distinction, in respect to this attempted control, from other products in common use which enter into free competition, subject, of course, to reasonable regulations prescribed for the protection of the public and applied with appropriate impartiality."[38]

One who reads only the above majority opinion in that case is rather impressed by the finality of the Court's language, but he will be equally impressed by the vigorous and heavily documented dissenting opinion written by Mr. Justice Brandeis and concurred in by Mr. Justice Stone. This minority opinion no doubt carried much weight in decisions on subsequent cases involving public regulation.

Mr. Brandeis' most telling argument was directed to the point that the power to determine how far public regulation should be extended into the various fields of business enterprise should be

[35] Okla. Sess. Laws 1925, c. 147.

[36] *New State Ice Co. v. Liebmann*, 285 U.S. 262 at 273 (1932).

[37] *Ibid.* at 277.

[38] *Ibid.* at 279.

left to the discretion of the legislature:

"Whether the local conditions are such as to justify converting a private business into a public one is a matter primarily for the determination of the state legislature. Its determination is subject to judicial review; but the usual presumption of validity attends the enactment."[39]

"In my opinion, the true principle is that the State's power extends to every regulation of any business reasonably required and appropriate for the public protection. . . . Moreover, the Constitution does not require that every calling which has been common shall ever remain so. The liberty to engage in a common calling, like other liberties, may be limited in the exercise of the police power."[40]

He went on to show that in the past businesses which had been common callings have later been declared public businesses by legislatures.

The general import of the minority opinion of Brandeis in 1932 became the majority opinion in the Nebbia case four years later. In fact, in the latter case, the Court was even more sweeping in its language:

"*So far as the requirement of due process is concerned, and in the absence of other constitutional restrictions, a state is free to adopt whatever policy may reasonably be deemed to promote public welfare and to enforce that policy by legislation adopted for its purpose.*"[41] (Italics supplied.)

If this edict of the Supreme Court is to be interpreted literally, what constitutional limitation would estop a state, or a municipality, from adopting a unified system of distributing fluid milk either municipally owned or privately owned but municipally controlled? If the trend in court decisions is not completely reversed, we are reasonably sure that, whenever legislatures declare milk distribution to be affected with a public interest, such legislation will be sustained.

Several United States Supreme Court cases, one dating back more than 60 years, have helped lay the foundation which is still serving as a guide to the courts in determining the basis for public regulation. Three of these cases, *Munn* v. *Illinois*, the Wolff Packing Company case, and the West Coast Hotel case, will be summarized briefly. (The Nebbia case has already been discussed.)

The Munn Case. In 1870 Illinois passed legislation declaring all grain elevators and storehouses, where grain is stored for compensation, to be public warehouses and requiring that persons operating such businesses must procure a license from the proper state authorities and submit to regulation of rates to be charged for storage. Munn and Scott, managers of a type of warehouse falling under the above designation, violated the law by operating without a license. They were drawn into court, the litigation being carried to the United States Supreme Court and decided in 1876. This Court (7 to 2) upheld the regulation as being a proper exercise of the police power. Here the basic question at bar was not apparently the power of the state to require a license to operate; that power seems to have been assumed. The issue was rather whether the limitation upon the legislative power of the state, as imposed by the Constitution of the United States, was such as to relieve the state of the right to fix maximum charges for storing grain. Mr. Chief Justice Waite pointed out that the very essence of government suggests:

"the power to govern men and things. . . .[42] Every statute is presumed to be constitutional. The courts ought not to declare one to be unconstitutional, unless it is clearly so. If there is doubt, the expressed will of the legislature should be sustained."[43]

[39] *New State Ice Co. v. Liebmann*, Minority Opinion, 285 U.S. 262 at 284 (1932).
[40] *Ibid.* at 302–3.
[41] *Nebbia v. New York*, 291 U.S. 502 at 537.
[42] *Munn v. Illinois*, 94 U.S. 113 at 125 (1876).
[43] *Ibid.* at 123.

The concept, "affected with a public interest," was the structural foundation upon which the Court rested this case and many others involving the power of a state to regulate business:

"Property does become clothed with a public interest when used in a manner to make it of public consequence, and affect the community at large. When, therefore, one devotes his property to a use in which the public has an interest, he, in effect, grants to the public an interest in that use, and must submit to be controlled by the public for the common good, to the extent of the interest he has thus created. He may withdraw his grant by discontinuing the use; but, so long as he maintains the use, he must submit to the control."[44]

The Wolff Packing Company Case. In this case, as in the New State Ice case previously mentioned, the Court denied the right of control which was specified in the legislative enactment. The Kansas legislature passed an act in 1920[45] declaring the following enterprises to be affected with a public interest:

"First, manufacture and preparation of food for human consumption; second, manufacture of clothing for human wear; third, production of any substance in common use for fuel; fourth, transportation of the foregoing; fifth, public utilities and common carriers."[46]

The legislation was challenged and the case carried to the High Tribunal.

At the outset the Court classified those businesses clothed with a public interest and over which may be imposed regulation of varying degrees of completeness:

1. Those occupations recognized from earliest times as being exceptional in that a public interest was attached to them. Included in these occupations are inns, cabs, grist mills, etc., which were regulated by colonial legislatures.

2. Those occupations which operate under authority of a public grant giving them special privileges and requiring, in turn, that they render service requested by any member of the public. These include the common carriers and our more typical public utilities.

3. Those businesses which have developed such a peculiar relationship to society that, from the public point of view, regulation of them has become desirable or necessary. The last group is more distinctly a product of our complex society than are those in Classes 1 and 2. In this group would be included the regulation of hours and wages; health and sanitary regulations; regulation of monopolies, including those which involve regulation of margins to be charged by commission companies and brokers; the present type of regulation of fluid milk prices; and a host of others.[47]

Here again the Court mentioned:

"That the mere declaration by a legislature that a business is affected with a public interest is not conclusive of the question whether its attempted regulation on that ground is justified."[48]

The sharp contrast between the language of the majority opinion in the Wolff Packing case and that in the Nebbia case 12 years later is at first glance so decided that a reader is inclined to ask what was responsible for the change in the philosophy of the Court.[49] The decision in the Wolff Packing case turned largely on legalistic interpretation, the concept of public welfare being relegated to the background. In the Nebbia case the relative importance given to the two concepts was reversed. The Court in the Wolff Packing case made the historical observations that:

"It has never been supposed, since the adoption of the Constitution, that the business of the butcher, or the baker, the tailor, the wood chopper, the mining operator or the miner was clothed with such public in-

[44] *Ibid.* at 126.
[45] Kansas Laws 1920, Spec. Sess., c. 29.
[46] *Ibid.*
[47] Cf. *Wolff Packing Co. v. Industrial Court*, 262 U.S. 522 at 535 (1922).
[48] *Ibid.* at 536.
[49] One must recognize, of course, that whereas the point of view of the Court may have changed, the import of the two acts was not exactly parallel.

terest that the price of his product or his wages could be fixed by State regulation. It is true that in the days of the early common law an omnipotent Parliament did regulate prices and wages as it chose, and occasionally a Colonial legislature sought to exercise the same power; but nowadays one does not devote one's property or business to the public use or clothe it with a public interest merely because one makes commodities for, and sells to, the public in common callings of which those above mentioned are instances."[50]

The West Coast Hotel Case. Among recent cases, the statement of the United States Supreme Court in the West Coast Hotel case (1936) is highly significant. The Court reiterated the position it had taken in the Nebbia case two years earlier, calling attention to the fact that:

"the general subject of the regulation of the use of private property and of the making of private contracts received an exhaustive examination [in the Nebbia case], and we again declared that if such laws 'have a reasonable relation to a proper legislative purpose and are neither arbitrary nor discriminatory, the requirements of due process are satisfied'; that 'with the wisdom of the policy adopted, with the adequacy or practicability of the law enacted to forward it, the courts are both incompetent and unauthorized to deal'; that 'times without number we have said that the Legislature is primarily the judge of the necessity of such an enactment, that every possible presumption is in favor of its validity and that though the court may hold views inconsistent with the wisdom of the law, it may not be annulled unless palpably in excess of legislative power'."[51]

In deciding this case, the Court relied mainly upon the Munn case of 60 years' standing.[52]

Neither the Nebbia case nor the West Coast Hotel case was decided on the basis of an existing economic emergency requiring temporary legislation. The decisions rested, instead, largely upon the principle of public purpose and public welfare. As long as the present philosophy of the Court toward public regulation continues, these two cases will have a profound influence in future Court decisions concerning the right of the state to enact and carry out legislation involving "public regulation for the common good."[53]

Importance Placed upon Public Welfare

When and if a case comes before the United States Supreme Court involving the regulation of milk under public utility control, including the exclusive franchise feature, the question of the legality of the franchise will probably turn on the degree of public interest involved. Specifically, in the opinion of the Court, will the fostering of competition or of monopoly best promote the public welfare? On the basis of recent decisions the likelihood would seem strong that the present personnel of the Supreme Court would sanction regulation under a legislatively created monopoly. For example, in the West Coast Hotel case (1936) the Court was clear in its position:

"There is no absolute freedom to do as one wills or to contract as one chooses. . . . Liberty implies the absence of arbitrary restraint, not immunity from reasonable regulations and prohibitions imposed in the interest of the community. . . .

"But the liberty safeguarded is liberty in a social organization which requires the protection of law against the evils which

[50] *Wolff Packing Co. v. Industrial Court, supra* n. 47 at 537. See also Charles Bunn, "Public Price Fixing and Due Process," 195 *Annals of the American Academy*, January, 1938, Supplement, p. 46.

[51] *West Coast Hotel Co. v. Parrish*, 300 U.S. 379 at 398 (1936).

[52] *Munn v. Illinois, supra* no. 42.

[53] For a discussion on the Federal Agricultural Marketing Agreement Act, especially as it affects milk regulation, see 17 *New York University Law Quarterly Review* 86–96 (November, 1939). Also see an interesting article, G. Lloyd Wilson and Joseph R. Rose, "Recent Trends in Public Utility Control," 29 *American Economic Review* 746–59 (December, 1939).

menace the health, safety, morals, and welfare of the people."[54]

On the basis of the position taken in the above case and others adhering to the same philosophy in which the public welfare received major emphasis, the Court could logically rule that the law governing the distribution of milk as a public utility would also turn on the question of public welfare.

In several United States Supreme Court cases reference was made to the idea of monopoly, but in none of the cases does a direct distinction appear to have been made between regulation permitting an exclusive franchise or license and a provision for a license to operate with no specified number of businesses permitted in an area. In the New State Ice Company case, for example, reference was made to the condition of monopoly but the case cannot be said to have turned on that point. It does, however, give sufficient warning that a proposal to limit the number of concerns permitted to enter a field in the so-called common callings may encounter serious objections by the courts.

To be sure, regulation, with or without the exclusive franchise, comprises the license feature which, on the face of it, presumably involves the power of the regulatory body to decline the granting of a license to a prospective operator or to revoke the license from an actual operator in event of violation of the provisions set down by the legislative act.

If the distinction between operation under regulated competition and regulated monopoly involves form or method of operation rather than legal principle, then, since the first method of regulation is not repugnant to the Constitution, on the basis of the Nebbia and the West Coast Hotel cases, the legality of a regulated monopoly could be logically defended as coming within the same rule. There would seem to be no difference in the fundamental principle involved in the two. There may be, of course, a distinction in the state statutes or even in the ordinance of the city or municipality which would permit one method but bar the other.

In the legislative acts of the states which the writer reviewed, a license was required of all milk distributors in the field, although the intent of the acts seems not to have been a limitation of distributors to any particular number. There was, however, nothing which the writer was able to interpret to the effect that licenses must be granted to all who applied.

Provisions for revoking licenses may vary with the method of control and the language of the act, but some provision for revocation in the case of non-compliance is in reality the heart of the purpose of this kind of license feature.

Interpretation of the Constitution by Court

Two fundamental bases of interpretation, or measuring sticks, have guided the Court in arriving at its decisions in cases involving public regulation to be imposed upon business, industry, and trade:

1. A purely literal, legalistic interpretation of the Constitution in which the Court has relied rather heavily upon former cases in support of the conclusion; and

2. A less literal interpretation with greater emphasis upon the concept of public purpose and public welfare—the assumption being that the writers of the Constitution intended it to be an instrument under which society would be per-

[54] *West Coast Hotel Co. v. Parrish, supra* n. 51 at 392.

mitted to meet gradual or violent social and economic adjustments.

Under the first interpretation, the Constitution and the Amendments are assumed to be a document fixed and unchangeable; under the second, a living instrument. The assumption of a judicial fixity in a dynamic social order, when carried to its logical end, strikes one as a process which will eventually lead to economic chaos. If the Constitution is to be so interpreted that a society is estopped from adjusting itself to conditions arising out of the increasing social and economic complexities, then, by the same process, a democracy may fix itself in a judicial strait-jacket which will sooner or later lead to governmental strangulation.

This should, however, not be construed as a defense of judicial sanction of all new and experimental legislation. Legislation always carries with it the dangers of being entirely ill-conceived, economically unwise, or poorly adapted to meet existing conditions. Thus one may appreciate the shortcomings attached to a philosophy at the opposite extreme whereby the judiciary takes the unequivocal position that "a state is free to adopt whatever policy may reasonably be deemed to promote public welfare and to enforce that policy by legislation adapted to its purpose."[55]

The late Mr. Justice Cardozo in speaking of fundamental judicial conceptions and justice calls attention to the conflicting principles with which courts are faced:

"One principle or precedent, pushed to the limit in its logic, may point to one conclusion; another principle or precedent, followed with like logic, may point with equal certainty to another. In this conflict, we must choose between two paths, selecting one or other, or perhaps striking out upon a third, which will be the resultant of two forces in combination, or will represent the mean between extremes."[56]

Referring to a particular case, Cardozo summarized his philosophy by saying: "in the end, the principle that was thought to be most fundamental, to represent the *larger and deeper social interest*, put its competitors to flight. I am not greatly concerned about the particular formula through which justice was attained."[57] In his opinion, a purely legalistic interpretation of the Constitution as it applied to everyday problems was virtually impossible. "There is," he said, "in each of us a stream of tendency, whether we choose to call it philosophy or not, which gives coherence and direction to thought and action. Judges cannot escape that current any more than other mortals."[58]

The discussion to this point suggests that probably a more accurate prediction could be made by knowing the members of the Court than by knowing in detail all the history of similar Court decisions. In the words of Chief Justice Hughes prior to his appointment to the Supreme Bench, "*We are under a Constitution, but the Constitution is what the judges say it is.*"[59]

Although the courts can find both legal precedence and logic for supporting legislation to make milk a public utility operated as a unified system under an exclusive franchise, they will not be unmindful of the practical limitations and difficulties of this type of control,

[55] *Nebbia v. New York, supra* n. 41 at 536.

[56] Benjamin N. Cardozo, *The Nature of the Judicial Process* (New Haven: Yale Univ. Press, 1937), p. 40.

[57] *Ibid.* at 42. (Italics supplied.)

[58] *Ibid.* at 12.

[59] Edwin S. Corwin, *The Twilight of the Supreme Court* (New Haven: Yale Univ. Press, 1934), p. 181. See also Charles Evans Hughes, *Addresses* (New York, 1908), p. 139. The reader is also referred to a lengthy bibliography entitled, "The Constitution of the United States," 185 *Annals of the American Academy* 190 (May, 1936).

and of the repercussions of legal sanction of such legislation. For example, producers' cooperative groups and producers individually have generally taken the position that public utility operation of milk distribution would redound to their disadvantage because of a loss of bargaining position. Accordingly, they can be expected to exercise all possible influence against this method of distribution. Many producer-distributors will insist upon their constitutional right to sell the product of their toil in a free and open market. Likewise, many consumers will resent a requirement that they purchase exclusively through a legislatively created monopoly. Especially in the smaller towns and cities they would insist upon their right to deal with individual distributors in obtaining their milk supply.

Clearly, these difficulties will exert a decided influence upon action of the courts in rendering their decision as to the legality of such legislation.

Influence of Economic Savings on Legality

If it can be shown that excessive waste inherent in the existing competitive system redounds to the public disadvantage, the economic outcome is similar to that which would prevail if a virtual monopoly existed. Either is contrary to the public interest. From a purely economic point of view it matters little whether the high price paid by milk consumers, in relation to that received by those who produce that same milk, is the result of unduly wasteful competitive methods of distribution or of unduly large monopoly profits. May there not be the same justification to protect the public against competitive waste as against unregulated monopoly profits? The courts have concerned themselves with the latter, but have not been required to give major attention to questions involving competitive waste. Summarily, assuming the legality will turn on the question of public welfare, then the issue will become primarily the possible economic saving under public utility operation.

The economic phases of public utility control of the milk distribution business have been a subject of study by the writer, the results of which it is expected will be published elsewhere. Space does not permit of a development here. Briefly, the possible savings resulting from an efficiently operated unified milk distribution system in cities of say 10,000 to 100,000 population would range in amounts varying from 1 1/2 to 2 cents or perhaps even 2 1/4 cents per quart of milk handled. Such savings would be made possible by (1) reducing the time spent in soliciting "new" patrons and in collecting customer accounts; (2) reducing the time spent delivering milk because of an elimination of duplicated milk delivery routes; (3) lowering the capital investment in buildings, machinery, and delivery equipment to "fit" the market needs, which reduction would bring about a corresponding decrease in the items of depreciation, repairs, insurance, and taxes; and (4) decreasing the number of salaried officers and managers and, to a lesser extent, profits.

To a family using two quarts of fluid milk daily, this would mean a saving of $11.00 to $15.00 annually. An item of this size can hardly be dismissed as unimportant to a large family of low or even medium income. Suppose this amount were saved and expended for the purchase of additional milk, other foods, clothing, or other necessities, it might contribute toward improving the family's health and vigor. In the end, would it not contribute toward the public health and welfare?

These savings are, however, predicated upon several assumptions—namely, (1) the investment in land, plant, and equipment for the new system would be prudently and honestly made or, more specifically, that all units of the plant or the equipment would be of such size, construction, type, and quality as to permit of relatively high efficiency and corresponding low cost of operation; and that the prices for which these were purchased represent economic values void of all semblance of favors, bribes, excessive profit or graft; (2) that the management of the new system would maintain substantially the same degree of efficiency permitted in the operation of that system as is now being maintained by each of the milk distributors under the competitive system; and (3) that the enterprise will be free from political influence in deciding policies to be established, appointments of management, prices to be paid and received for milk, and standards and type of services rendered in the operation of the enterprise.

Summary

So far the United States Supreme Court has not ruled upon the legality of a type of control in the milk business involving the exclusive franchise feature, although such rulings have been made in the accepted public utility fields. Court decisions to which one must look for precedents are not such as will provide a dependable indication of what position the Supreme Court may take on the question of the exclusive franchise feature of control of milk distribution. Nevertheless, there would seem to be sufficient legal support for the position that the legislatures have power either to grant exclusive franchise to a private corporation to process and distribute milk, or to delegate to the city or municipality the power to perform the function itself through municipal ownership. The outcome of the decision will depend largely upon the particular case brought before the Court and upon the philosophy of the majority of the Supreme Court members at the time the case appears for decision. In the final analysis it will doubtless turn mainly upon the question of whether costs of the inherent competitive wastes are serious enough so that, in the opinion of the Court, the public welfare of the people in a city will be improved through control and unification of the milk distribution system. If the Court favors a philosophy of increased social control in the interest of public welfare, it can with consistency reach a decision supporting a legislative act imposing control similar to that now in force over the more typical public utilities.

Finally, the degree of success of public utility operation and regulation will be dependent in no small measure upon political considerations. Even though it can be shown that such savings could be brought about, this is not proof of the fact that they would be carried out if public utility control operating as a unified system of milk distribution were put into effect. If it were certain that those responsible for the management of a city—or state—were thoroughly qualified to direct a business such as milk distribution and that they could also be depended upon to operate it strictly in the public interest with no personal or political considerations, then it would be relatively easy to predict the extent of savings which *would* actually be brought about. But can we always be confident that such conditions will be carried out? Only experience can give answer to this question.

A Diagnosis and Suggested Treatment of an Urban Community's Land Problem

By EDMUND N. BACON*

THERE are an estimated 30,000,000 vacant lots in the United States. These present a problem of far greater magnitude than is generally recognized. A large proportion of these lots are tax delinquent, and thus a public charge. This demands the formulation of a public policy in respect to them, usually by the state legislature.

In the past this policy has customarily taken the form of postponement of any permanent disposition of these lands, in the hope that they would automatically return to the tax rolls. This policy has not worked out as hoped, and the whole situation is rapidly coming to a head.

The great difficulty any law-making body faces in dealing with this problem is the almost complete lack of any coherent policy on the part of cities as to what should be done with this land. It is basically a municipal problem, and its existence seriously affects the municipal economy. If cities do not know what to do about it, how can state legislatures be expected to develop constructive policies?

This study[1] deals with one particular city, Flint, Michigan, which is typical of most medium sized cities. The problems which the case study presents have a bearing on those of the largest cities, and the proposals for solution have general application.

Because of its uncontrolled development following the industrial expansion early in the century, Flint is now spread over 30 square miles with 44% of its subdivided lots vacant. Of these, 12,257, or 43% of the vacant parcels, have reverted to the state for tax delinquency. Present construction is principally outside the city limits, a trend which can only result in serious depopulation of the city.

In the face of a shrinking population to carry existing tax burdens, and reduced value of real property as a base for tax revenue, the operating costs of the city are increased by reason of the scattered development. In the long run this condition can lead only to increased taxation per person, or serious curtailment of city services and institutions.

This study is an analysis of the extent and character of the problem, with recommendations for its solution.

Historical Growth

Map I shows the evolution of the land pattern of Flint at various dates. It was developed from historical maps which exist for approximately 15-year intervals. Factual data (Table I) for corresponding years were derived partly from these maps and partly from city plat maps and United States Census data, augmented by studies by Ernest M. Fisher.

1859. As Map I shows, the original settlement of Flint grew around the commercial center at the crossing of the main travel route to the north and the

* City Planner, Philadelphia, Pa.

[1] It presents the major part of a report authorized and approved by the former City Planning Board. The research for this study was executed through WPA funds, and the report prepared by the writer. Since its adoption, the Planning Commission has been reorganized by a charter amendment, and as yet it has taken no final action on the recommendations of this report, so that they cannot be said to represent a policy generally accepted by the city. The report itself, however, indicates a growing interest in these problems, and through the basic facts presented may pave the way for an officially adopted, constructive land policy of some sort.

Flint River. By 1859 the economic future was assured and an ambitious plan for expansion had been laid out, paralleling the wagon road. The adjacent area was divided into blocks containing lots of ample size (66×165 feet). At this time only 37% of the 1,672 lots had been built upon.

1873. The town grew rapidly under the stimulus of lumbering activity aided by the new railroad to Saginaw. The population had doubled. Several lumber-

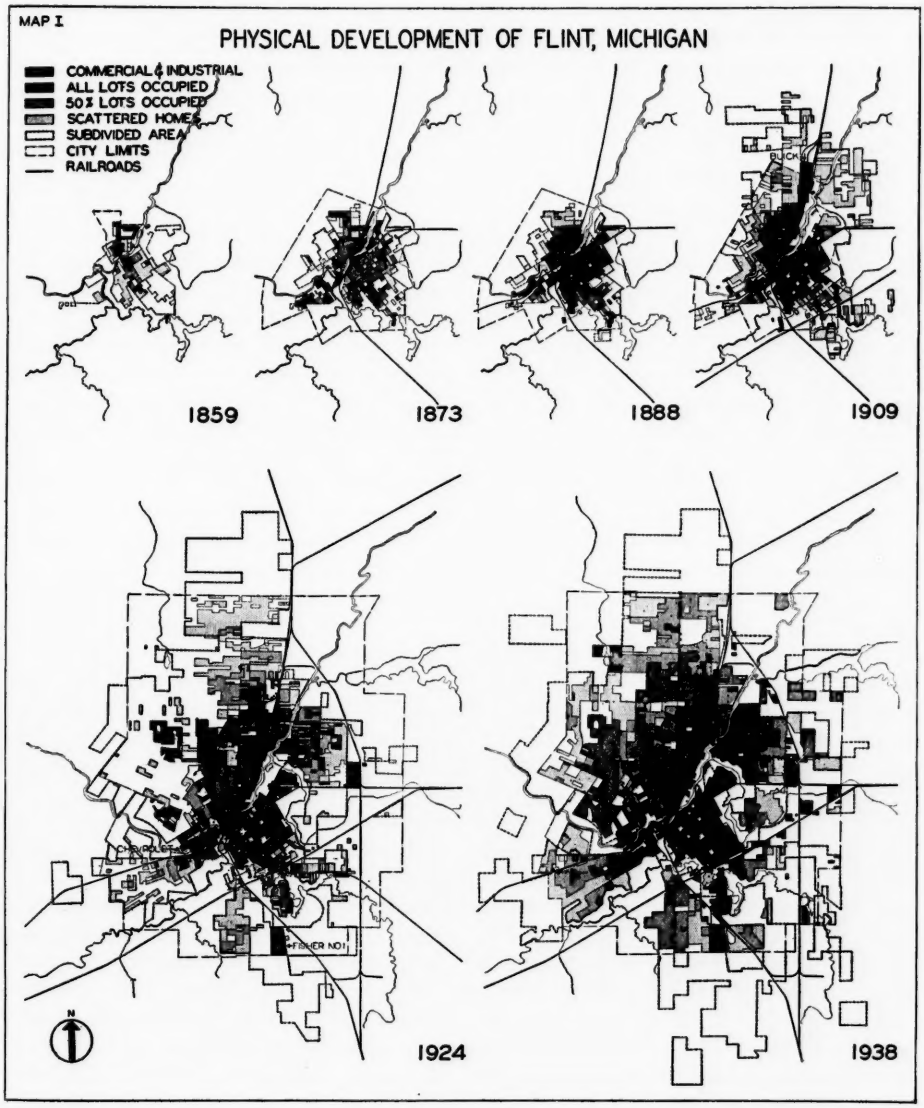


TABLE I. POPULATION AND LOT DATA, FLINT, MICHIGAN, 1859–1938.

Date	Population	Number of Lots	Lots Occupied	Lots Vacant	Per Cent Vacant	Typical Lot Size (Feet)	Minimum Lot Frontage (Feet)
1859*	2,950‡	1,672	612	1,060	63%	66×165	66
1873*	6,600§	3,984	1,507	2,477	62	66×132	50
1888*	9,540§	4,035	1,910	2,125	53	48×150	48
1909*	38,550‡	15,230	7,239	7,991	52	40×110	40
1924*	113,300§	57,749	23,044	34,705	60	40×100	35
1938*	160,000¶	64,063	35,537	28,526	44	45×100	40
1924†	129,491§	75,574	26,337	53,237	66		
1938†	191,995¶	90,324	42,425	47,899	53		

* Subdivisions within City of Flint only.
† Subdivisions within regional area, including City of Flint and Burton, Flint, Genesee, and Mt. Morris Townships.
‡ Nearest U. S. Census.
§ Interpolated from U. S. Census.
¶ Estimated.

ing mills had sprung up along the Flint River. New houses were built on the vacant lots in the older sections of the city and 2,312 new lots were added, forming a ring of vacant area around the town. Some of the new lots were smaller than those originally planned, but none was less than 50 feet in width. The city limits were extended to include the new areas.

1888. Flint had now matured into a stable and secure community. Commercial and industrial activity adequately supported the gradually growing population. The city limits remained as before, and for 11 years no further subdividing occurred. The new building was limited to filling in and developing the land already platted. The large lots gave privacy and recreation space, the houses were well constructed, and the streets were lined with shade trees. The entire community was compact and orderly. At this point the city achieved the soundest physical layout of its history.

1909. At the turn of the century the city was stirred by the new idea of manufacturing motor-driven vehicles. By 1909 the Buick Motor Company was firmly established and had built a new plant to the north of the city. During the 30 years prior to 1903 only 429 new lots had been recorded, but immediately upon the promise of industrial expansion subdividing activity assumed feverish proportions. In the next seven years 15,432 lots were added, more than four times all the lots in the entire city up to that time. These were scattered over a huge area surrounding the Buick factory. The new lots were also smaller and for the first time 40-foot lots appeared. Also the new practice of scattering houses over the subdivision was begun.

1924. By this time the climax had been reached. Under the influence of industrial expansion the population had trebled and the number of lots increased five times. There were now 53,000 vacant parcels, or enough to care for three times the existing population. These lots were characteristically 40 ×100 feet; a few thousand were 35 feet in width, although this width was abandoned in later subdividing. The new subdivisions formed a vast area encircling the city, both within and without the city limits, sparsely settled or entirely vacant. The city limits were extended to an area five times that of 1909, to include many of these subdivisions.

1938. The period of industrial expansion has passed and the city is now facing a stabilization at the present population level. It has 28,526 vacant lots within the city limits and a total of 47,899 within the region. The problem of the future disposition of this land is the subject of this study. From this point, however, the study is confined to the area within the city limits because of the limitation of this research project. The entire region should be treated thoroughly in a future study.

Distribution of Single-Family Lots

The total area within the city limits of Flint is 19,114 acres. Of this, 14,166 acres are developed for urban use, i.e., occupied by subdivided lots, streets, public parks and open spaces, and commercial or industrial properties. There remains an undeveloped area, 4,948 acres in extent, covering 26% of the total city area.

The distribution of subdivided lots occupied by single-family dwellings within the developed area is shown on Map II. The scattered white spaces around the business center show the usual infiltration of rooming houses and converted apartments into original single-family areas. In Flint this has not spread far, and in general the older areas are compactly developed with single-family homes.

Completely surrounding the city is a broad band, about a mile wide, of the newer subdivisions developed entirely with scattered housing. In the Corunna Road sector to the southwest and the Fenton Road sector directly south, only 50% of the lots are occupied, and vacant lots are spread throughout the entire area. The Court Street section to the east is only 25% occupied; west of "Modern Housing" is an area with only 8% of the lots occupied.

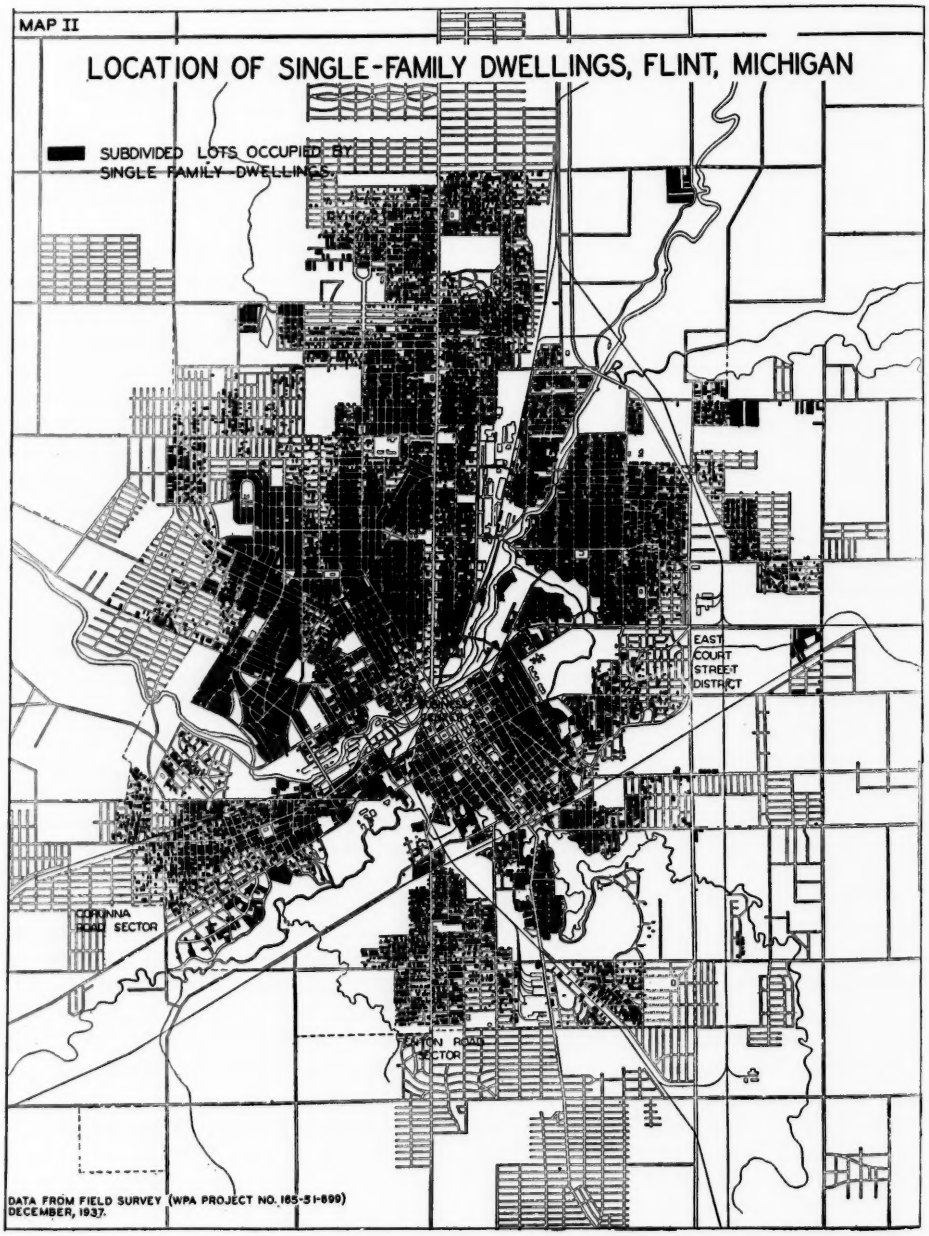
This pattern of scattered building is characteristic of all subdivisions developed in Flint since 1910, with the single exception of General Motors' Modern Housing project, conspicuous on the west side of the city. Over 9,000 houses, or ¼ of all the dwellings in Flint, are built in this scattered manner, in subdivisions which include over ½ the entire subdivided area. This characteristic is of extreme importance in the current and future life of the city.

This pattern of development was caused by past subdividing methods. Building activity is regarded as increasing the salability of adjacent vacant lots. The subdivider, faced with the problem of finding purchasers for his many lots, would encourage the building of a few houses in each block of his subdivision. Ordinarily he would then sell the remaining vacant parcels to small investors, who anticipated a profit from resale of the lot to the eventual builders. This practice would have been successful were it not that subdividing so greatly exceeded the ultimate market for building lots. As a result, thousands of the lots were never built upon, and all the newer subdivisions are now only partially filled.

From the home owners' point of view this would appear to be an advantage; for the purchase price of a small lot he is surrounded by plenty of open space. However, if the subdivision achieves its objective and all the lots are filled, this is only a temporary advantage. If it does not, there is danger that the adjacent lots will be opened to inferior construction, and the value of his home will thereby suffer. There is also the danger that cessation of building at a sparsely developed stage will stamp the subdivision as derelict, and the resale value of the home be greatly reduced. In general, this type of subdivision is a serious detri-

ment to the security of property values.

From the city's point of view it presents a serious problem in current operating expense. The costs of police and fire protection are partly proportional to the area covered, and in this



case the cost is far greater than it would be were there fewer subdivisions but completely developed ones. Since 1912 the city has spent $11,805,343 of current operating funds in these two departments alone. Even a small proportional current saving would represent a large accumulated sum.

In garbage and ash collection the most distant house must be reached, and it is obviously more expensive when the trucks must pass several vacant lots for each house served. Flint has 527 miles of streets to be maintained, and of these over 200 miles run past vacant lots. Since 1912, $1,797,153 have been spent on refuse collection, and $1,461,439 on dirt street maintenance. In both cases there has been sheer wastage of a large part of these funds because of the miles past vacant lots. The same applies to sidewalk repair and sewer maintenance.

From the consumer's point of view the people of Flint must also bear the costs of added miles in the delivery of milk and groceries, added miles of electric and gas lines to be maintained, added miles of bus service per person, and many other similar costs. In short, scattered vacant areas reduce the security of property values, are a constant and heavy drain on municipal operating expenditures, and increase the costs of other services for which the Flint consumers must pay.

Condition of Dwellings

The physical condition of the homes is of prime importance, both as an indication of neighborhood stability, and of the need for replacement building in the future. A housing survey made in the city in 1934 showed:

Condition of Dwellings	Number	Per Cent of Total
Dwelling units in good condition	15,893	45.1%
Dwelling units needing minor repair	13,394	38.0
Dwelling units needing structural repair	5,015	14.2
Dwelling units unfit for human use	679	1.9
No record	267	0.8
Total	35,248	100.0%

From these data the dwelling units in each block were weighted according to the following scale: good condition—1.0; minor repairs—0.8; structural repairs—0.4; unfit for use—0.0. Map III shows the comparative rating for each block, with good to poor condition grading from light to dark.[1a]

Although this map shows considerable decay around the business section, the factories, and the railroads, in general the older areas of the city are in good condition. The poorest structural ratings are principally in the newer subdivisions around the periphery of the city, mostly developed within the past 20 years. The very rapid deterioration in much of the newer construction results from inferior building methods. This indicates that thousands of homes will become unfit for use within the next few years, and must be replaced. This necessarily means population movement and the direction of that movement is of great importance.

Investigation of new building within and without the city limits shows a startling trend. Within the city limits from 1930 to 1937 only 950 new dwelling units were provided, or an average of 135 per year. In these seven years this number fell 4,000 short of replacing obsolete existing houses, estimated on the basis of a 50-year life per house. In the same period approximately 2,084 homes, or more than twice the number constructed in Flint proper, were built just outside the city limits in adjacent

[1a] Originally this map showed the condition of dwellings in somewhat greater detail, but its reduction to present dimensions necessitated omission of some detail.

subdivisions, in Burton, Flint, Genesee, and Mt. Morris townships (Table II).

It is evident that replacement of deteriorated buildings in Flint is being carried on outside the city limits. This is also reflected in a study of the homes

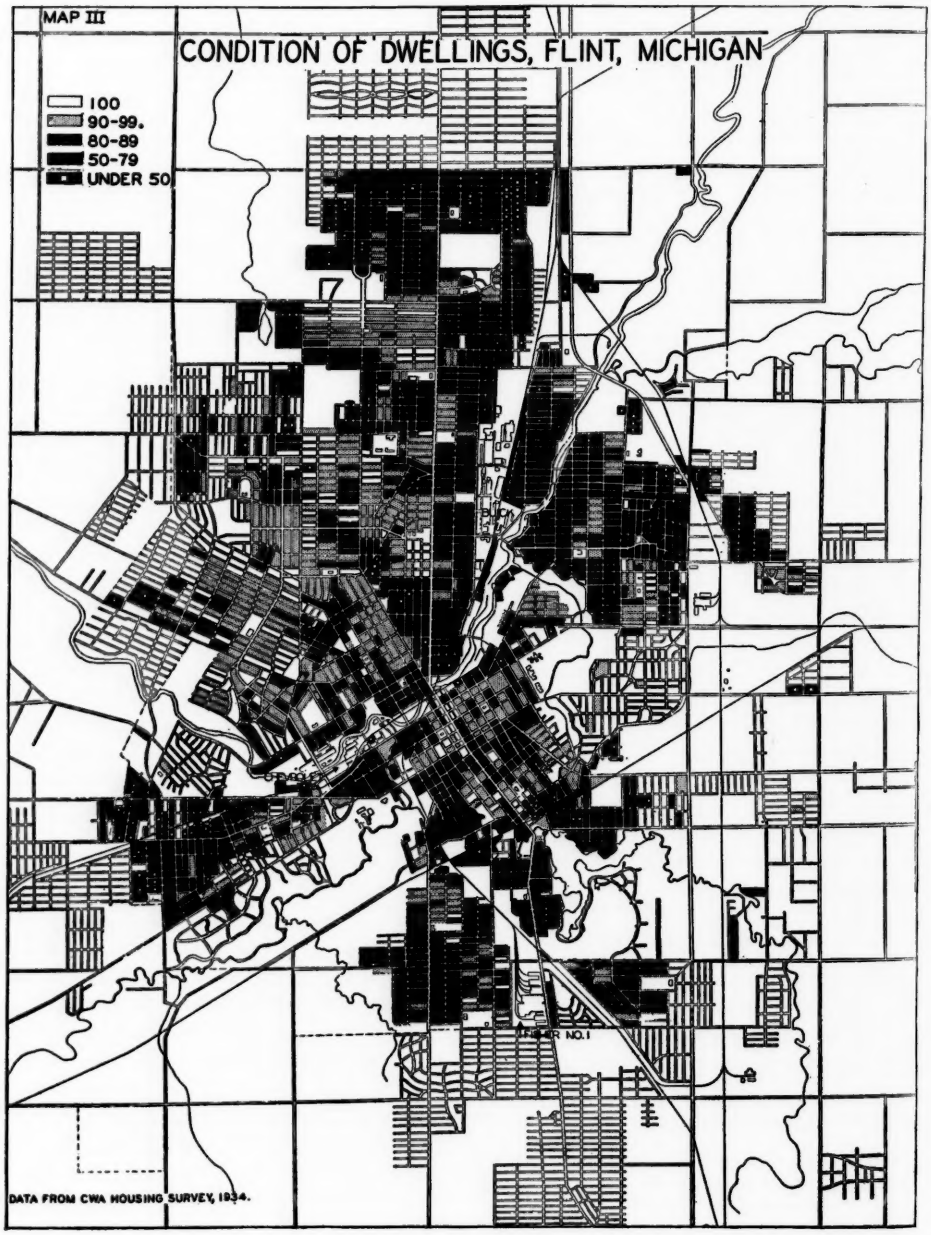


TABLE II. POPULATION AND HOUSING DATA, 1930–1937

Item	Flint City Limits	Adjacent Subdivision
1930 Population*	156,492	20,708
Homes Added (1930–7)	950†	2,084‡
Persons per Family	4.10	4.10
1937 Population	160,387‡	29,256§
Population Increase		
Amount	3,895‡	8,548‡
Per Cent	2.5%	41.2%

* U. S. Census. ‡ Computed.
† Actual. § From school census.

of factory workers. A count of the 30,859 workers employed in the four major Flint plants in 1936 showed that 2,822 (9.0%) lived in the subdivisions just outside Flint, and 3,887 (12.6%) lived in neighboring towns. In short, more than 1/5 of the factory workers who derived their incomes in Flint lived outside the city limits. On the assumption that each worker represents a family of 4.10 people, the following distribution is shown:

	Number	Per Cent of Total
Population within city limits of Flint	160,387	78.0%
Population outside city limits living in adjacent subdivisions	29,256	14.2
Families of workers employed in Flint living outside adjacent subdivisions in neighboring towns	15,937	7.8
	205,580	100.0%

Thus 22% of the people who derive their livelihood in Flint contribute nothing to it in taxes and this condition is increasing at an accelerated rate. The further deterioration of thousands of Flint homes will hasten this tendency. A continuation of the present trend of building outside the city limits, accelerated by rapid obsolescence within the city, will lead to a serious depopulation of Flint.

Extent and Usability of Vacant Subdivided Land

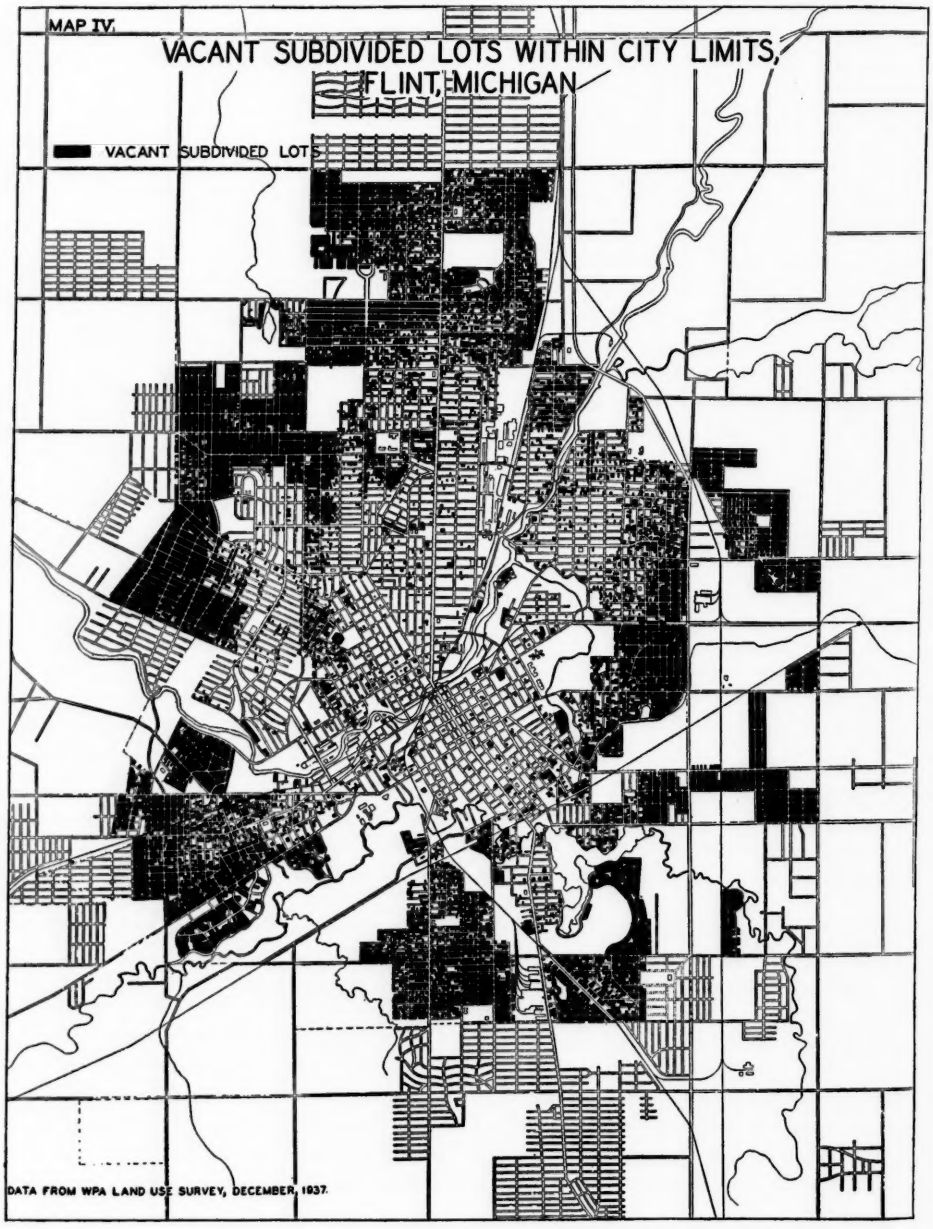
The land assets of the city are shown on Map IV. All the black areas are subdivided vacant lots, of which 28,526 are within the city limits and cover 3,259 acres or some five square miles. They constitute 44% of all subdivided lots within the city. These lots would be sufficient for nearly double the present population, but population forecasts promise very little, if any, increase. No extensive new industries are likely, and those now present will probably stabilize at current average production. There may be an increase in the service activities, in which Flint is abnormally low, and in retail and wholesale trade, but these would probably only compensate for a possible decrease in numbers industrially employed.

Since no major population increase is likely, the greater part of these lots will never be used. However, it has already been shown that thousands of houses will soon deteriorate to the point of being unusable, and will have to be replaced. If this replacement is carried on outside the city limits, as is the tendency at present, Flint will face a serious depopulation. Why is the vacant land within the city so unattractive for private building?

The Federal Housing Administration Underwriting Manual, Section 605, states: "A most important group of factors which affect mortgage risk is the one which embraces the relationship between the physical property and the neighborhood in which it is located." Certainly if this is true of a mortgage, it is equally true for an individual who invests his own capital in his own home.

As Map IV shows, the entire area of vacant lots is sprinkled with houses. These determine the neighborhood char-

acter of the intervening vacant lots. Comparing this map with Map III, it is also seen that at least 80% of all these vacant lots lie in the peripheral belt where the houses are in the poorest condition. This means that a few scattered



inferior houses have stamped the greater part of the land assets with the character of a deteriorated neighborhood. By the principles of good business, expressed by the FHA, as well as sound common sense, it would be poor judgment to pour good money for new construction into the bottomless pit of a blighted neighborhood. Hence the migration to new areas.

This insecurity of neighborhoods, resulting from scattered development and rapid spread of blight, is one of several factors that makes mortgage lending in Flint a high-risk proposition. Equally with the deterioration of the house itself, the deterioration of the surrounding neighborhood before expiration of the period of the loan will mean a capital loss to the mortgage investor. Frequent experiences of this sort have led to high interest rates and mortgage financing charges to cover the risk. This increases the costs of shelter to the consumer.

Financial Aspects—Utilities

Map V shows the vacant lots serviced by sewer or water lines, or both, and Table III shows the actual data for vacant as well as tax delinquent lots. There are 19,791 vacant parcels serviced by both sewer and water, and 3,219 more serviced by one or the other. At the conservative estimate of $2.00 per running foot, this represents an unused investment of approximately $1,700,000. Adding the cost of sidewalks at $1.00 per foot and street grading at $1.00 per foot gives a total unused investment exceeding $3,000,000.[2]

It costs just as much to run sewer and water lines past 20 vacant lots as if they contained 20 houses. If each lot is occupied, the cost will be shared by 20 families. If only one lot is occupied, it costs 20 times as much to service it, and someone must pay the difference. Either the subdivider and the speculative buyers pass the cost along to the one family that builds, thus greatly increasing its shelter cost, or they take the loss themselves or they default on the payments. In the latter case the City of Flint must make up the difference. In any case, the cost must be ultimately borne by Flint citizens.

The city has actually paid a very large direct subsidy to subdividing. Of the 19,791 vacant lots served by both sewer and water, 41% are delinquent on taxes prior to 1935. General city funds of $623,000 have been paid directly to cover default on special assessments and the present outstanding special assessment refunding bonds total $756,000.[3] Of the $11,418,185 that has been expended for sewers and storm sewers by the city engineering department

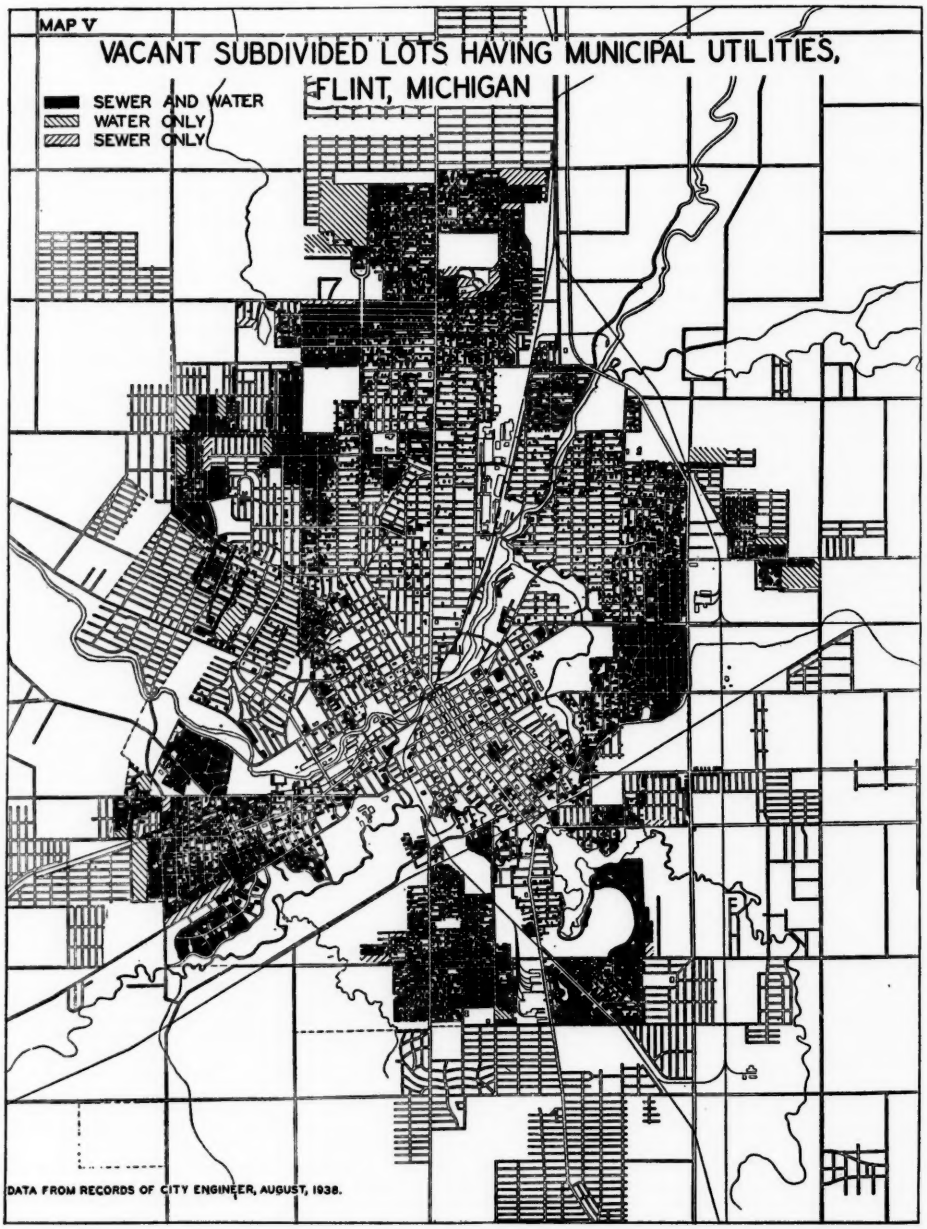
[2] Unit cost estimates supplied by the city engineer of Flint.

[3] As of February, 1939.

TABLE III. VACANT LOTS SERVICED BY UTILITIES.

Utilities	Vacant Lots		Vacant Tax Delinquent Lots		
	Number	Unused Investment in Sewer and Water Lines (estimated)	Number	Per Cent	Unused Investment in Sewer and Water Lines (estimated)
Sewer and water	19,791	$1,583,280	8,088	40.8%	$647,040
Water only	2,288	91,520	1,203	52.6	48,120
Sewer only	931	37,240	289	31.0	11,560
Neither	5,516	—	2,677	48.5	—
Total	28,526	$1,712,040	12,257	43.0%	$706,720

since 1915, $5,585,983 (49%) was paid directly by the taxpayers through general city obligation bonds; an additional $3,473,232 (30%) comes from federal funds through the WPA; and only $2,358,970 (21%) from special assess-



ments and other sources, making no allowance for special assessment delinquency. (See Table IV.) This shows a direct public subsidy of the vacant lots.

The very great proportional costs of providing scattered homes with utilities is seen in a recent WPA project which cost $1,123,000 for only the sanitary sewers. The total assessed valuation of all buildings in the project area is $1,192,310. When the water mains are included, a great deal more value was buried underground than existed above it. This project covered 153 blocks, with a total of 4,142 lots of which 2,424 (58%) were vacant, and 967 were delinquent on taxes prior to 1935. The cost per occupied lot for the sewer lines was $650, or slightly below the average assessed valuation of the houses. Within this area, 388 houses needed major repairs, and 141 were classified as unfit for human use by the 1934 housing survey. If all the public funds sunk into sewers past vacant lots could have been used to provide decent housing above the ground where utilities already exist, far greater value per dollar would have been received.

Despite this enormous area of 20,000 vacant lots provided with utilities, the current building in Flint is taking place almost entirely outside the city limits in unsewered subdivisions. Eventually these areas will also have to be sewered, and much greater public funds will be sunk beneath the ground in utilities, while thousands of feet of pipes within the city limits lie unused. From a business point of view this endless multiplication of sewers and water lines represents wasted expenditure which is a serious drain on public funds.

Tax Delinquent Land

Map VI shows in black the properties which were put on sale at the May, 1938 Genesee County Tax Sale for delinquent taxes from 1928 to 1935 and which were bid in by the state for lack of other purchasers. Within the city there were 14,866 such descriptions, of which 13,667 were subdivided lots. Of these, 12,257 (90%) were vacant. They cover 1,509 acres and represent a total of $2,748,171 in unpaid back taxes. This sum would be sufficient for the entire operation of the city for a year and a half.

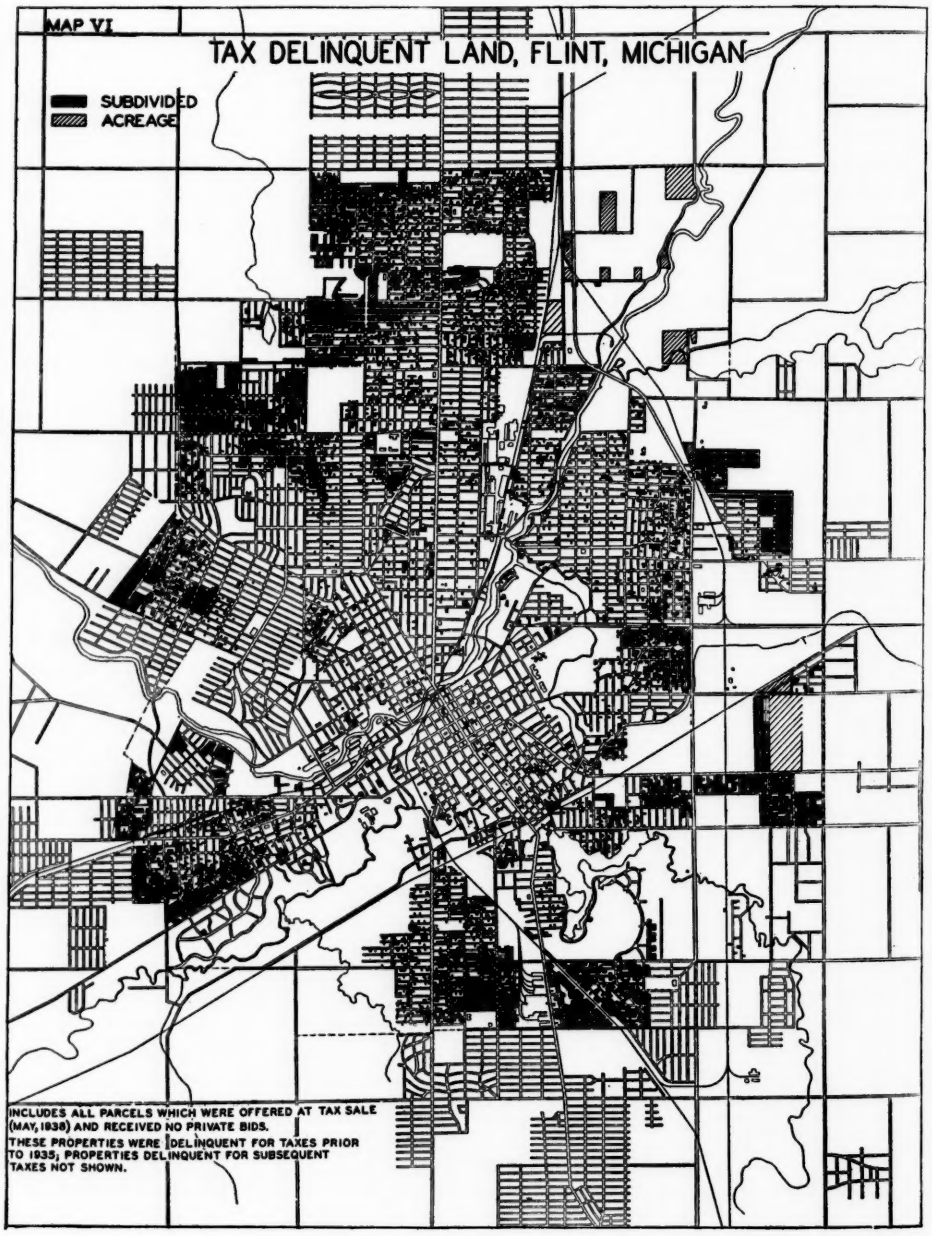
Eighteen months after the tax sale, in this case October, 1939, such parcels as have not been redeemed by their original owners revert to public ownership, and the title is vested in the state. Originally all land belonged to the state. The Flint area was originally granted by the state to the Indian descendants of Jacob Smith, early settler. After passing through many ownerships, almost 15,000 descriptions of this land again return to the state.

In order to understand this process, it is necessary to examine the history of a vacant lot. The only reason for subdi-

TABLE IV. EXPENDITURES FOR SEWERS, 1915–1939.

Source	Sanitary Sewers		Storm Sewers		Total	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
City bonds	$2,954,483	53.3%	$2,631,500	44.8%	$5,585,983	48.9%
Special assessment—other	1,272,017	22.9	1,015,121	17.3	2,287,138	20.0
City—WPA sponsor	30,299	0.5	41,533	0.7	71,832	0.6
Federal WPA	1,290,822	23.3	2,182,410	37.2	3,473,232	30.5
Total	$5,547,621	100.0%	$5,870,564	100.0%	$11,418,185	100.0%

viding in excess of need is to make a profit from the sale of excess parcels to speculative investors. The only reason for buying a lot as an investment is to anticipate additional profit from its sale to the ultimate consumer. Since the



lots are developed in excess of need and therefore must remain strictly non-productive for some time, the investor must also figure both the interest on his investment and the taxes which are constantly accumulating. The longer it is held the greater the amount he must charge in addition to the original cost to cover these items. The ultimate consumer must pay both profits and the accumulated deficits over the non-productive period. It is obvious that, with 28,000 vacant parcels awaiting purchasers, most of these will have to run scores of years before they are sold. It is also obvious that ultimate consumers will be financially unable to pay the deficit which has accumulated over so many years, because this will have exceeded the real value of the lot several times. So the obvious and inevitable happens; the speculative investor loses his lot to the taxing units on tax default.

The situation is complicated, however, by the state law expressed in Act 155, Public Acts 1937. This law provides that the land may be resold at a "scavenger" sale two years after the original sale for any bid above 25% of the assessed valuation. It further provides that any one with an interest in the property at the time of sale may redeem his property for a sum equal to the highest bid, to be paid on equal installments over a 10-year period. What this does, in effect, is to surrender the public equity in the land, wipe out back taxes, and return the property to the original speculator for a down payment of 2.5% of its value. In the case of a $200 lot, typical of large sections of Flint, this would require a payment of $5.00. The buyer may then hold the lot for another three years with no further tax payments, at which time it would again be up for tax sale, and two years following, or five years after the original $5.00 payment, he may retrieve the parcel for an additional $5.00, if this method is repeated.

The taxpayer has already heavily subsidized this lot by direct payments from public funds for the utilities, which in many cases approximately equal the value of the lot. The taxpayer takes the loss in increased cost of city operation resulting from speculative subdivision of the land and consequent scattered building. He is also endangered by a heavy population migration from the city, caused by this land condition. If this continues, he will have to bear a proportionally heavier share of the total city tax burden. It is very much to his interest that this land be used for building rather than for speculative holding, so that it will produce tax revenue. It has already been shown that a principal deterrent to its use for building is diversified ownership of the lots and scattered building.

It is still possible that the city may exercise its lien and retain control of some portion of this land. The law provides that home rule cities may withhold the land from the scavenger sale for one year. It also provides that the cities may hold such land as is not sold at the scavenger sale, and use it for any public purpose, and at the end of 10 years dispose of it as the municipality sees fit. The law might also be amended to give the city fuller control in a shorter time.

There are many constitutional questions involved, still to be thrashed out in the courts. Whatever the method, the ultimate objective of turning this land back to private productive use would point to centralized rehabilitation of this land by municipal effort, and the only rational basis for determining the extent to which this is constitutionally possible is first to clarify wherein lies the greatest public benefit.

Conclusions and Recommendations

The following conclusions are derived from the previous analysis:

1. Flint is burdened with a serious oversupply of vacant, subdivided land.
2. The scattered housing on this land greatly increases current municipal operating costs.
3. The several million dollars of public funds which have been spent for utilities for these areas make their use a public responsibility.
4. The heavy tax delinquency on these areas makes them non-productive for tax revenue.
5. The accumulated back taxes and the scattering of deteriorated houses are serious deterrents for new building in these areas.
6. In spite of the huge vacant areas within the city, new building occurs principally outside the city limits, a trend which will eventually result in serious depopulation of the city.

In order to return the land to productive use the back taxes will have to be written off and the city will have to take the loss. If the land is returned to the original owner stripped of taxes, the land situation will remain as at present. Neighborhood blight will still prevent building, migration outside the city will continue, and the land will remain non-productive to both the speculators and the city.

The cause of non-productivity lies outside the control of the individual lot owner, and can be removed only by centralized reassembly and replanning of neighborhoods, removal of the causes of blight, and creation of sound land values. This demands concerted action, through the organization created for concerted action, the city government. Therefore it is necessary for the city to retain control of tax delinquent land in order to return it to productive private use. In this way the city may receive return from the land in which it has so heavy an investment.

Through continuous application of this policy for the future control and planned re-use of the tax delinquent land, the city may achieve three separate but interrelated objectives which are of vital concern to the tax structure:

A. Reduction of scattered development on the outskirts of the city and filling in of the gaps in close-lying areas to reduce municipal operating costs.

B. Aiding in building within the city limits to provide better houses, increase local prosperity, and provide additional assessed valuation for tax revenue.

C. Reduction of further migration from the city and re-attracting of families back into the city limits.

The actual pattern of the tax delinquent land (Map VI) shows that it falls into two definite groups: (1) areas close to the factories and business center which are from 50 to 70% delinquent, and (2) outlying areas up to 90% delinquent.

Through its control of tax delinquent land the city may rehabilitate the most delinquent close-lying areas, remove neighborhood factors which are causing blight, write off accumulated back taxes which are a cause of high land price, and offer the land at reasonable terms for private building with the stipulation that it be developed on a planned neighborhood basis. This would tend to encourage investment of capital in housing, protect the mortgage investor through greater neighborhood security, and create more stable assessable values. The tax returns from this land in productive use would far outweigh the loss in back taxes on the land when vacant. This method would not only discourage further migration from the city, but would also tend to further concentrate development within the city.

This would be the beginning of the achievement of the first objective—reduction of city operating costs. If the

close-lying vacant areas are rehabilitated and all new construction takes place there, the outlying blighted areas will gradually be replaced closer in. Again through its control of tax delinquent land, the city may prevent further building in the most sparsely developed and most delinquent outlying areas, eventually acquiring the entire subdivision and returning the land to productive farm use. This would materially reduce the area requiring city services, and consequently city operating costs.

Many of the simpler reasons given for migration outside the city limits may be overcome by the city's control of tax delinquent land. One of these is the desire for larger lots. Obviously, with 5½ square miles of vacant subdivided land, 1,509 acres of which are delinquent, there is plenty of land within the city limits for everyone. Delinquent subdivisions may be replatted into larger lots, and the outlying, unsewered subdivisions turned into small farms. Trees may be planted, and every advantage of the county offered within the city limits.

Less exacting building regulations within the county are frequently offered as a reason for the outward migration. This is a legislative matter, requiring determination of decent minimum standards for workers' housing, and equal enforcement throughout the county.

The most usual reason offered for moving into the county is lower taxes. From the workers' point of view this is often more imaginary than real. If, as a result, he lives three miles from work, assuming the very low figure of 2 cents per mile and 40 working weeks, transportation will cost him $24.00 per year. This is more than the entire yearly tax rate on a $1,000 house in the city at the 1938 rate, which has been constantly declining. By the time he allows the differential for the taxes he is now paying in the township, he will probably discover there is no saving at all, and he would be better off financially had he built on one of the hundreds of vacant lots within walking distance of the factories. For the sum previously spent for transportation he would receive better services for his family.

In any case the low township taxes are likely to be temporary. The first families moving in will receive the benefits of lower taxes, but as hundreds follow and the subdivision becomes built up, all utilities and services which caused the high taxes in the city will also be required here. New sewers, water mains, and schools will have to be built, and the families living here will have to pay the bill. Already some of the townships have a higher tax rate than that of Flint. The family finds itself tied to a home far from town, with transportation costs eating into the budget, and taxes as high as or higher than in the city. Whereas in Flint the utilities and schools are already 50% paid for, here the family is saddled with a debt which is just beginning.

When all these facts are generally understood, and stable attractive land values offered within the city, the trend of migration outside the city limits may be largely reversed.

Future Program

The specific program for achieving these objectives includes:

1. Adoption of the necessary legislative measures giving the city full control of tax delinquent land, to develop, sell, lease, or hold such land as a long-range program may require.

2. Formulation of a long-range land utilization policy making fullest use of the tax delinquent land and Public Works programs by the City Planning

Commission, in close cooperation with the Housing Commission and other governmental agencies. This plan should include the classification of all areas[4] in the city into five groups:

A. Neighborhoods in good condition to be maintained and protected.

B. Concentrated blighted neighborhoods to be rehabilitated.

C. Concentrated slum areas to be cleared and rebuilt.

D. Scattered blighted areas to be rehabilitated for new building or abandoned.

E. Sparsely settled, unsewered, outlying subdivisions to be abandoned and returned to agriculture or municipal forests.

3. Continuous application of this program to all future city activities.

The entire program may be achieved at very little extra cost over a period of years because of the obsolescence of existing houses and the need of their replacement. The total effect of this program will be a great economy by reason of the stabilizing of present good property values, and the replacement of deteriorated property by new construction within the city limits. This will stabilize and increase the value of real property and its consequent tax return. It will reduce the area of the city requiring municipal services, and consequently operating costs, and permit better value per tax dollar received.

[4] Actual determination of these areas would require detailed study beyond the scope of this report.

The City of Flint, through expenditures of the taxpayers' money, has painstakingly built up the utilities and institutions necessary for a well rounded, functioning community. These include sewers, a water system, fire stations, hospitals, parks, and schools. Bonds in the amount of $12,096,569 have been issued by the city since 1913, and are being paid for by its citizens. An additional $11,000,000 is invested in the school system, and $7,000,000 in the water plant. Over $7,000,000 has been expended on public works by the WPA, 36 cents on the current tax dollar goes to pay for these bonds, and thus every citizen in Flint has a vested interest in these institutions. The peak has passed and the amount of tax money necessary to pay this debt is decreasing. Municipal bonds and school bonds are already 50% paid off, and will entirely disappear in 1962. The combined efforts of the city with its services and the industries with their employment have made the community and given its land value. It is to the interest of everyone that this land be used in such a way as to take most advantage of the utilities and institutions they have provided.

Many elements are necessary to do this, but the constructive use of tax delinquent land as a municipal land reserve is the first and most fundamental step.

II. Financial and Depreciation History of the Utah Power and Light Company*

By LIONEL W. THATCHER†

THE first installment of this article contained a discussion of the excess book cost, as well as of the original cost, of the Utah Power and Light Company's property and plant. Its depreciation policies were examined and a reconstructed depreciation reserve, more in keeping with sound accounting practice, was presented. In the light of these data an estimate of the return was calculated at the rate of 7% on the original cost of the company's properly. It now remains to consider the excess revenues of the company during the period covered by this study, the rates of return on property and plant calculated on various bases, and the returns on stock equities.

Excess Revenues

After determining the total revenue requirements for Utah Power and Light Company, which includes operating expenses, taxes, uncollectible bills, rentals, adjusted depreciation expense, and a 7% rate of return, a comparison was made with the total operating revenues collected per Company books. This comparison represents a rather interesting picture. Here is an example of a utility which, over a 24-year period, has collected from ratepayers of the state $6,097,489 over and above the amount needed to cover all expenses of operation and a 7% return on the net original cost of property and plant and estimated working-capital requirements. Table V also showed that, except for the depression period (1931 to 1936), the average revenues since the advent of regulation in 1917 have exceeded the requirement for operating expenses and a 7% return by more than $750,000 a year. For the period from 1924 to 1929 inclusive, the excess revenue collected over the revenue requirement was well over $1,000,000 a year.

Another point worth noting is that, in spite of the creation of the Public Service Commission in 1917, the excess revenues increased steadily until 1929. Furthermore, the increase in rates granted by the Commission in 1921 is reflected by the sharp increase in excess revenues subsequent to that year.

By drawing on information relating to rates of return on total and common stock equities to supplement the foregoing analysis, the following conclusions may be emphasized. Because of excessive trading on the equity and questionable financial policy, the Company has presented, in the years prior to the depression, a favorable earnings statement. In fact, it has paid $7,200,000 in common stock dividends to its holding company and in addition had paid supervision, engineering, and financing fees to Electric Bond and Share Company which in reality represented substantial profits to the organization.[6] Moreover, about $4,000,000 of guaranteed interest payments to Utah Light and Traction Company, which is really a form of profits to the Power Company, has been included

* For the first installment of this article see 15 *Journal of Land & Public Utility Economics* 448–55 (November, 1939).

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[6] 70th Cong., 1st Sess., Sen. Doc. No. 92, Pt. 45.

as operating expenses. The Company has been able to show these earnings by: (1) financing so as to get all actual money invested in the system through long-term debt and preferred stocks at relatively low interest and dividend rates; (2) not amortizing bond discount and expense and stock selling expense, both incurred largely to get low interest and dividend rates; (3) burying these bond discounts and costs of selling stock in the property and plant accounts; and (4) failing to record the true cost of operation because of inadequate provisions for depreciation.

Rate of Return on Utility Plant

Rates of return on utility plant have been computed on average property and plant determined on the basis of (1) book cost, (2) original cost, and (3) original cost minus the reconstructed depreciation reserve. The rates of return on these various bases are shown in Table VI and are obtained by dividing net operating income from operations by each of these bases respectively. The rates of return calculated on the first two bases are really only trends, and are at variance with accepted doctrines inas-

TABLE VI. RATES OF RETURN ON PROPERTY AND PLANT:* UTAH POWER AND LIGHT CO., 1913–1936

(000's Omitted)

Year	Net Operating Revenue per Company's Records	Average Book Cost of Property and Plant		Estimated Original Cost of Property and Plant		Estimated Net Original Cost of Property and Plant		
		Amount	Rate of Return	Amount	Rate of Return	Amount	Net Income after Deduction for Deficiency in Depreciation	Rate of Return
1913	$ 823	$29,212	2.82%	$ 9,228	8.92%	$ 8,185	$ 639	7.81%
1914	829	40,604	2.04	15,387	5.39	14,197	521	3.67
1915	1,441	46,051	3.13	20,827	6.92	19,332	1,024	5.30
1916	1,970	48,739	4.04	23,415	8.41	21,545	1,501	6.97
1917	2,381	53,125	4.48	27,640	8.62	25,241	1,828	7.24
1918	2,673	56,692	4.72	31,139	8.58	28,161	2,050	7.28
1919	2,541	57,800	4.40	32,247	7.88	28,639	1,896	6.62
1920	2,820	58,793	4.80	33,240	8.48	28,981	2,155	7.44
1921	3,084	59,775	5.16	34,222	9.01	29,348	2,399	8.18
1922	3,330	61,398	5.42	35,845	9.29	30,435	2,613	8.59
1923	4,017	63,802	6.30	38,249	10.50	32,314	3,252	9.06
1924	4,334	66,780	6.49	41,227	10.51	35,577	3,510	9.86
1925	4,745	69,519	6.83	43,966	10.79	37,617	3,865	9.28
1926	5,147	71,001	7.25	45,448	11.32	38,321	4,238	11.06
1927	5,189	73,138	7.10	47,585	10.91	39,688	4,237	10.68
1928	5,435	76,503	7.10	50,950	10.67	42,464	4,416	10.40
1929	5,575	78,835	7.07	53,285	10.46	43,918	4,509	10.27
1930	5,180	80,566	6.43	55,013	9.42	44,912	4,080	9.08
1931	4,572	81,975	5.56	56,422	8.10	45,533	3,443	7.56
1932	3,843	82,396	4.66	56,843	6.76	44,938	2,706	6.02
1933	3,167	82,254	3.85	56,701	5.59	44,416	2,033	4.58
1934	3,321	81,783	4.06	56,230	5.91	43,242	2,196	5.08
1935	3,384	81,663	4.15	56,138	6.03	42,209	2,261	5.36
1936	4,090	82,054	4.98	56,864	7.19	41,978	2,953	7.03

* Accountants' Report, 1936, *op. cit.*

much as in both cases the undepreciated rate-base was used without adjusting depreciation to a sinking fund basis as was the book operating income, which was subject to inadequate depreciation charges.

Working capital has not been included in the base upon which rates of return have been calculated because no detailed studies of working-capital requirements have been made. Furthermore, the inclusion is not particularly important since the primary purposes of the computations of return in this section are to show the trend of returns earned and the spread between returns indicated on a book basis and after elimination of excess costs of property and provision for more adequate depreciation. Moreover, inclusion of working capital would have little effect.

On all bases of computation, ratios of net operating revenues (after payments of rentals for leased properties) to property and plant for the period as a whole were lowest in 1914 and highest in 1926. After the 1926 peak the rates tended downward until 1933, after which the upward trend was resumed.

The outstanding feature in the trend of rates of return on the total property and plant as shown by the Company's balance sheet is the increase of almost 1% (from 5.42% in 1922 to 6.30% in 1923) which followed the rate increase granted by the Public Utilities Commission in 1921.

After elimination of the ascertained write-up carried in the Company's property accounts, the rates of return were more than doubled for the first four years of operation shown in Table VI. Thereafter, growth of properties by construction and acquisition was practically free of excesses, if any at all, over cost. As a result, the ratio of increase in rates caused by deduction of excess prices paid from total property and plant decreases. Rates after deduction of excess over the cost of properties shows about the same general trend as the rates on the total property and plant as shown on the Company's books. The rate increase in 1921 was followed by a sharp rise between 1922 and 1923 in the rate of return calculated on the original cost figure for property and plant. Naturally this rise was greater than when computed on the book cost basis.

After adjusting net operating income for the deficiency in depreciation expense and after subtracting the reconstructed depreciation reserve from original cost of property, the rates of return were decreased considerably from those on the original cost basis. Nevertheless, with the possible exception of a three-year period (1933–1935), the rates of return, after the advent of regulation in 1917, are clearly in excess of the maximum "fair return" established by most commissions throughout the country. The rather low rates of return of 1931 and 1932 are explained by the greater adjustments in net income made necessary because of the reduction in depreciation allowance in those years (see p. 451 of Part I cited above).

Rates of Return on Stock Equities

Rates of return on total stock equity and common stock equity have been computed, based respectively on total stock equity before and after deductions for excess costs of properties and on common stock equity as shown by the Company's books. No rates of return on common stock equity after deductions of excesses and correction for deficiency in depreciation are shown because, as seen in Table VII, the excess, except for four years, was above the book value of common stock equity. In other words, the common stock equity was algebraically

negative; therefore, no rates of return could be computed.

Rates of Return on Total Stock Equity. Rates shown for total stock equity in Table VII are based on the net income available for dividends as shown by the Company's records and as adjusted for deficiencies compared with: (1) the total stock equity (book surplus included) as shown by the Company's records at the end of the year; (2) total stock equity as described in (1) above less the excess costs of properties as determined by the accountants of the Public Service Commission; and (3) total stock equity as described in (1) and (2) above less the estimated deficiency in the depreciation reserve as determined by the writer.

Based on the Company's records, rates of return on total stock equity, before the depression period, ranged from 1.30% in 1914 to 6.06% in 1928. In 1934 the rate of return reached its lowest point (0.77%), but in 1935 and 1936 it returned to a more normal percentage. After deductions for "write-ups," the rate of return, compared with that determined on book costs, was practically tripled until 1923 and doubled every year thereafter, except for the brief period of two years during the depression. Table VII shows that the rate of return fell below 6% only in the last five years of the 24-year period covered in this study.

TABLE VII. RATES OF RETURN ON TOTAL STOCK EQUITY:* UTAH POWER AND LIGHT COMPANY, 1913–1936
(000's Omitted)

Year	Total Capital Stock Equity per Company Books	Total Capital Stock Equity after Deductions for Excess Cost	Total Capital Stock Equity after Deduction for Deficiency in Depreciation Reserve	Net Income Applicable to Total Stock Equity		Rate of Return on Total Stock Equity		
				Per Books	Adjusted for Additional Depreciation Expense	As per Company Books	After Deduction for Excess Cost	After Deduction for Deficiency in Depreciation Reserve
1913	$36,384	$ 9,289	$ 9,092	$ 639	$ 454	1.76%	6.87%	5.03%
1914	34,981	6,481	5,976	454	146	1.30	7.01	2.45
1915	39,293	11,906	10,985	755	339	1.92	6.34	3.08
1916	39,103	12,254	10,879	1,063	595	2.72	8.67	5.46
1917	39,591	11,246	9,434	1,088	636	2.75	9.68	6.74
1918	40,614	14,355	12,125	1,151	728	2.83	8.02	6.01
1919	41,891	15,934	13,158	989	639	2.37	6.21	4.86
1920	41,658	15,516	12,554	950	861	2.28	6.12	6.85
1921	41,891	15,945	12,894	1,129	1,045	2.70	7.08	8.10
1922	42,739	15,956	12,729	1,269	1,152	2.97	7.92	9.05
1923	43,422	16,695	13,390	1,663	1,598	3.83	9.96	11.93
1924	47,630	20,273	16,857	2,113	1,988	4.44	10.42	11.79
1925	51,237	24,749	20,157	2,496	2,317	4.87	10.09	11.41
1926	51,676	25,675	21,618	3,038	2,829	5.88	11.88	13.09
1927	52,951	25,807	21,616	3,008	2,757	5.68	11.66	12.75
1928	53,621	26,294	21,785	3,249	2,930	6.06	12.36	13.45
1929	55,743	29,630	24,756	3,313	2,947	5.94	11.18	11.91
1930	57,031	30,310	25,035	2,922	2,522	5.12	9.64	10.07
1931	57,026	31,232	25,329	2,507	2,078	4.40	8.03	8.21
1932	57,182	31,449	24,710	1,747	911	3.06	5.57	3.69
1933	57,908	32,677	25,504	610	176	1.05	1.87	0.69
1934	57,626	32,221	24,623	446	22	0.77	1.39	0.09
1935	58,474	32,921	24,900	608	185	1.04	1.85	0.74
1936	59,210	33,657	25,199	1,357	920	2.29	4.03	3.65

* Accountants' Report, 1936, *op. cit.*

In exactly 12 out of the 24 years, the return was above 8%. After reducing the net income available for stock equity by the amount of deficiency in the depreciation expense, the rate of return was lowered in some years and raised in some other years over the return as adjusted for excess costs. The fluctuating rates of return were attributable to the changing depreciation allowance made by the Company. After all adjustments, the average rate of return for the period 1921 to 1931 inclusive was 11.08%. During the years 1933 to 1935, the return dropped materially, being only .09% in 1934 and .69% and .74% in 1933 and 1935, respectively. However, for the entire period (1921 to 1936, inclusive) the average return earned was 7.13%.

Rates of Return on Common Stock Equity. The rates for common stock equity (Table VIII) are based on earnings applicable to common stock compared with common stock equity computed as described above for total stock equity. Inasmuch as the net income applicable to common stock equity is that income available after provision for full preferred stock dividends, whether they are paid or not, it was necessary to adjust the net income for the delinquent preferred stock dividends.

Rates of return on common stock equity, as shown by the Company's books, after paying interest, full dividends on preferred stocks, other appropriations from surplus, and federal taxes, ranged from .06% in 1915 to 5.83% in 1930.

The par value of common stock has not changed since 1915. Moreover, all common stock outstanding since organization of the Company (except directors' qualifying shares) have been owned by the parent company, Utah Securities Corporation or its successor, Electric Power and Light Corporation. The parent company then has put no additional funds into the business except the earnings accumulated in surplus.

Table VIII shows that, except for a small amount in the years 1915, 1916, 1929, and 1936, there never was a positive common stock equity after making proper deduction for inflation in capitalization attributable to excess of book cost over original costs of properties acquired and for deficiency in depreciation reserve. Notwithstanding this fact, recorded surplus and surplus reserves accumulated from earnings have increased from approximately $271,000 at

TABLE VIII. RATES OF RETURN ON COMMON STOCK EQUITY: UTAH POWER AND LIGHT COMPANY, 1915–1936
(000's Omitted)

Year	Common Stock Equity per Books	Net Income Applicable to Common Stock Equity	Rate of Return on Common Stock Equity	
			Based on Company Books	After Deducting Inflation and Deficiency in Depreciation Expense
1915	$28,456	$ 16	.06%	*
1916	28,266	66	.23	*
1917	27,254	96	.35	*
1918	28,084	287	1.02	*
1919	28,504	68	.24	*
1920	28,271	13	.05	*
1921	28,254	181	.64	*
1922	27,682	265	.97	*
1923	27,865	578	2.07	*
1924	28,574	900	3.15	*
1925	29,181	1,067	3.66	*
1926	29,619	1,503	5.08	*
1927	29,935	1,435	4.80	*
1928	29,994	1,630	5.43	*
1929	31,261	1,665	5.33	*
1930	31,318	1,198	5.83	*
1931	31,314	†	†	*
1932	32,149	†	†	*
1933	32,176	†	†	*
1934	33,672	†	†	*
1935	33,515	†	†	*
1936	34,251	†	†	*

* No percentages shown because there was no positive equity upon which to compute rates of return.
† No net income when adjusted for delinquent preferred stock dividends.

the end of 1914 to approximately $7,500,000 at the end of 1936. By and large, it can be said that the Utah Power and Light Company has been financed with bonds, preferred stock to the extent of more than repaying Electric Bond and Share Company and Utah Securities Corporation for the cost of properties, and other assets acquired by Electric Bond and Share Company and later turned over to Utah Power and Light Company. As a result, the holding company has held all common stock over the entire period of 1913 to 1936 with no actual cash outlay.[7]

Not until 1925 were any dividends paid on common stock. Since that time common stock dividends were paid as follows:[8]

1925	$ 600,000	1929	$1,200,000
1926	900,000	1930	1,200,000
1927	1,050,000	1931	900,000
1928	1,200,000	1932	150,000
			$7,200,000

Since formation of the Company, then, dividends totaling $7,200,000 have been paid on the common stock which was originally acquired by the holding company at no cost (Table IX). During the same period the accounting has been such as to show an increase in common stock equity through surplus and surplus reserves of approximately $7,500,000. Actually, however, if the company had provided adequately for annual depreciation, it would not have reported such a surplus. In fact, if depreciation amounting to 2% of the original cost of properties had been provided, surplus would have been reduced to a deficit. To the extent that common stock dividends have been paid at the expense of providing adequately for depreciation, the capital has been impaired.

Although this entire analysis is premised upon original cost and adequate depreciation, the writer does not contend that properties acquired in arm's-length dealings at prices reasonably in excess of original cost should not be considered and given weight in prescribing reasonable rates or in valuation for security issues. However, the limitation of security issues to original cost finds a number of adherents. Certainly, the failure to provide for adequate depreciation should be taken into account, even though the estimates used herein may not be substantiated by comprehensive field investigations. The aim here has been to show the earnings, history, and trends of this property on the assump-

TABLE IX. SCHEDULE OF DIVIDENDS AND BOND INTEREST PAID BY YEARS:* UTAH POWER AND LIGHT COMPANY, 1912–1935
(000's Omitted)

Year	Common	7% Preferred	6% Preferred	Total Dividends	Bond Interest
1912	†	†	†	†	†
1913	†	$ 340	†	$ 340	†
1914	†	707	†	707	$ 367
1915	†	739	†	739	575
1916	†	997	†	997	896
1917	†	992	†	992	1,006
1918	†	864	†	864	1,034
1919	†	921	†	921	1,178
1920	†	937	†	937	1,212
1921	†	948	†	948	1,278
1922	†	1,003	†	1,003	1,575
1923	†	868	$217	1,085	1,855
1924	†	1,143	70	1,213	1,957
1925	$ 600	1,360	70	2,030	1,957
1926	900	1,465	70	2,435	1,957
1927	1,050	1,491	81	2,623	2,011
1928	1,200	1,474	146	2,820	1,961
1929	1,200	1,474	174	2,848	1,940
1930	1,200	1,474	250	2,924	2,108
1931	900	1,474	279	2,653	2,140
1932	150	1,454	250	1,854	2,140
1933	†	†	†	†	2,139
1934	†	242	42	284	2,090
1935	†	242	42	284	2,055
Totals	$7,200	$22,611	$1,691	$31,502	$35,432

* State of Utah Investigating Committee of Utah Governmental Units, "A Study of Utah's Public Utilities."
† No dividends paid.

[7] 70th Cong., 1st Sess., Sen. Doc. No. 92, Pt. 45, p. 1650.

[8] Accountants' Report, 1936, *op. cit.*, p. 176.

tions noted, as throwing light upon the efficacy of regulation in Utah.

In opposition to this type of financing, preferred stockholders residing in Utah filed suit in the supreme judicial court in equity of Maine. The preferred stockholders sought to compel the Electric Power and Light Corporation to pay $30,000,000 plus interest to the Utah Power and Light Company for the common stock issue of the latter Company.

It is stated in the report that the suit was brought on behalf of the preferred stockholders and the Utah Power and Light Company, which "refuses and neglects to bring said action in its own name." In brief the petition asked:[9]

1. That the Electric Power and Light Corporation, which holds all common stock of the Utah company, be required to make a full "disclosure and accounting of profits" received from the Utah Power and Light Co.
2. That the Utah Power and Light Company be required to make a similar accounting of all payments or security transfers to the Electric Power and Light Corporation.
3. That the Electric Power and Light Corporation be required to pay to the Utah company the par value of the common stock issue amounting to $30,000,000 plus interest from date of issuance, or that the common stock be cancelled. In the event of cancellation the suit asks for the return of $7,200,000 assertedly paid out in common stock dividends during 1925–32.
4. That the Utah Power and Light Company be enjoined from recognizing the validity of the right of the Electric Power and Light Corporation to vote the common stock, or of transferring such stock, or of paying dividends thereon.
5. That the common stock of the Utah Company was issued to "its promoters as secret, undisclosed and unlawful profits" and that it is invalid unless the par value of the stock is paid to the Utah Power and Light Company.

Pending a hearing, Supreme Court Justice James H. Hudson issued a temporary injunction preventing the voting or transfer of the common stock. On March 21, 1939, the case was dismissed. However, to the decree of dismissal the plaintiffs excepted and the action is now in the Law Court, continued to the December term, 1939.

After studying the financial policy of Utah Power and Light Company, it appears that the promoters of the Company were more interested in the financial set-up than in developing service through liberal rate policies. The financial structure was constituted in such a manner that it has been necessary for the holding company to squeeze every cent it could out of the operating company. The whole financial set-up brought such pressure upon Utah Power and Light Company for passing on revenue to the Electric Power and Light Corporation that it has been impossible for Utah Power to reduce rates sufficiently for adequate market development and unquestioned retention of its territory.

The analysis to this point has raised questions as to the efficacy of regulation in Utah, and this in turn has stirred up agitation for municipal ownership as a corrective in several of the larger communities. The results of this movement, its economic contributions, and its economic bases require further cost analysis which is not a part of this study.

[9] *Salt Lake City Tribune*, March 25, 1938.

Urban Land Department

MORTON BODFISH, *Editor*

Low-Cost Housing under the USHA Experiment

THE United States Housing Authority was set up in 1937 as an experiment in providing low-cost housing to the lowest income slum families and to increase activity in the dormant building trades industry. Eight hundred million dollars in loans from the USHA to local housing authorities was authorized and the government appropriated $28,000,000 a year from the Federal Treasury for subsidies to local authorities to assure the low-rent character of the projects. The theory was that the government should sponsor the building of new low-cost houses. To date, 347 projects have been authorized in 155 different communities, providing for a total of 130,000 families and the use of $581,966,000 of the $800,000,000 authorized.

Since so much emphasis is currently being placed on the slum problem and the need for more low-cost houses, it is important and necessary in light of the requests for larger USHA appropriations to study the operations of this huge housing agency and see just how successful it has been in sponsoring the building of truly low-cost homes.

The USHA experiment has been under constant attack on many fronts, one of the most fundamental of which is the matter of costs. The Administrator, Mr. Nathan Straus, has estimated that the funds appropriated in the original Act will provide for 163,200 families, and that the additional $800,000,000 being sought will enable the Authority to house a total of 423,000 families. With the USHA loan to local housing authorities equaling 90% of the total development cost, this will mean a capital expenditure of approximately $4,200 to rehouse one slum-dwelling family. The size of this figure immediately suggests a more thorough analysis of the capital costs of these supposedly low-cost public housing projects.

It is valuable to review briefly the cost experience of earlier public housing ventures. The USHA is the third of a series of recent experiments by the Federal Government to provide standard housing accommodations for low-income families. Under Title II of the National Industrial Recovery Act loans were authorized to limited-dividend housing corporations. In the seven projects approved for loans under that Act, the average total cost per dwelling unit was $3,372.[1] The houses built by the Public Works Administration cost, for the dwelling facilities alone, an average of $4,120 per family dwelling unit or $1,170 per room.[2] Comparable figures for projects financed by the USHA are approximately $3,660 per dwelling unit for contracts made during 1937 and 1938 and $3,130 for commitments made in 1939.[3] This indicates that the costs of construction in public housing projects have been reduced, probably as a result of constant pressure from opponents against this form of public assistance for shelter relief and the realization by government officials that the more that is spent for each family the fewer families that can be accommodated.

On the basis of these data the USHA appears to be successful in doing the job of providing low-cost housing, but this fact is not necessarily true. In the first place, the figures given above include only about 70% of the total capital outlay involved in the rehousing program; and, secondly, the PWA-built projects involved such tremendous and unnecessarily large outlays that almost any operation would appear favorable beside them. That the expenditures under the USHA program for dwellings to provide relief shelter to slum dwellers may still be excessive is suggested by a comparison of USHA costs with the costs of privately owned and financed houses being encouraged by the FHA and the Department of Commerce. These dwellings are to cost $2,500[4]

[1] "Status of Slum-Clearance and Low-Rent Housing Projects of the USHA," U. S. Housing Authority, Feb. 1, 1938.

[2] Does not include land costs or other project costs, such as street utilities, equipment for grounds, etc. (From Release No. 3304, U. S. Federal Emergency Administration of Public Works, PWA Press Section.)

[3] Includes construction cost of dwellings plus dwelling equipment and the local authority's architectural and overhead expenses applicable to dwelling construction and dwelling equipment. (See Table II, below.)

[4] A figure comparable to the figure on PWA and USHA dwellings mentioned above.

and under. These are homes for families able to support themselves and pay taxes, but will be cheaper and probably inferior in quality and conveniences to the homes provided out of government funds to slum families that need public assistance in order to secure adequate shelter.

In addition to the bare cost of erecting the houses and providing the necessary dwelling facilities, USHA's cost figures must include the costs of non-dwelling facilities, such as excavation, landscaping, streets and sidewalks, utilities outside the building wall, and the like, the cost of land for the actual site as well as land for future development, and the expenses of demolishing slum buildings on the project site. These expenses increase the cost of the houses over the bare dwelling facilities cost from 40 to 45%, to an average total cost of rehousing one family of $5,534 for projects approved up to December 31, 1938 and $4,575 for 1939-approved projects. In Table I is presented a percentage distribution of the items going into the total development cost of USHA-financed public housing projects.

Examination of the costs of USHA-financed projects shows that net construction costs[5] for projects approved as of December 31, 1938 averaged $3,148 per dwelling unit or $768 per room. For projects covered by loan contracts made in 1939 the net construction cost averaged $2,685 per unit. The total cost of dwelling facilities[6] for projects contracted for up to the end of 1938 was $3,668 per unit, and the total cost of new housing[7] was $5,098 per unit or $1,244 per room. The total development cost[8] of the 1938 projects averaged $5,534 per dwelling unit or $1,351 per room, and for the 1939 projects the average per unit was $4,575.[9] These costs are somewhat under the maximum permitted by law, which limits the average dwelling facility cost to $4,000 per unit in communities of less than 500,000 population and to $5,000 in larger communities. A detailed picture of these various costs is presented in Tables II, III, and IV. The costs there presented are *estimated* costs. Experience has not yet been sufficient to test actual costs against these estimated figures.

It is somewhat difficult to arrive at a fair comparison between the costs of privately financed and owned residential dwellings and USHA houses, yet it is helpful to compare the two in so far as it is possible in order to appraise adequately the reasonableness of USHA costs. Since there are no private enterprise cost figures comparable to the items of slum demolition and land purchased for future development involved in public housing projects, it is necessary to use for comparison the USHA figures presented in Table II. The privately financed dwellings most comparable to the USHA houses are the FHA rental housing projects financed under

[5] Includes construction cost of dwellings (i.e., structural, plumbing, heating, etc.).

[6] Includes net construction cost plus costs of dwelling equipment (such as ranges, refrigerators, screens, etc.) and the local authority's architectural, overhead, carrying, and contingency expenses applicable to dwelling construction and dwelling equipment.

[7] Includes total cost of dwelling facilities plus cost of land and non-dwelling facilities, such as cost of site improvements and of non-dwelling buildings.

[8] Includes total cost of new housing plus cost of slum buildings to be torn down on project site and total cost of land for future development.

[9] For sources see Tables II, III, and IV.

TABLE I. PERCENTAGE DISTRIBUTION OF THE COSTS INVOLVED IN USHA PUBLIC HOUSING PROJECTS*

(Based on projects covered by approved loan contracts as of December 31, 1938)

Cost Item	Per Cent of Total		
Land		6.81%	
Non-dwelling facilities		15.54	
Dwelling facilities:			
Equipment, architects, and overhead	60.37%		
Net construction	9.39	69.76	
Total cost of new housing			92.11%
Cost of slum buildings to be torn down on project site			7.50
Cost of land for future development			.39
Total Cost of Entire Project			100.00%

* Data from 1938 *Annual Report*, U. S. Housing Authority, Table IV.

TABLE II. PERCENTAGE OF USHA-AIDED PROJECTS SHOWING ESTIMATED NET CONSTRUCTION COSTS PER UNIT*

Net Construction Cost per Dwelling Unit	Year Contract Approved	
	Up to December 31, 1938	1939
Under $2,000		3.76%
$2,000 and under $2,250	2.88%	9.77
2,250 and under 2,500	4.31	18.80
2,500 and under 2,750	9.35	23.31
2,750 and under 3,000	14.39	19.55
3,000 and under 3,250	27.34	21.80
3,250 and under 3,500	25.18	2.26
3,500 and under 3,750	10.79	
3,750 and under 4,000	2.88	.75
4,000 and under 4,250	2.88	
Total	100.00%	100.00%
Weighted Arithmetic Mean	$3,148	$2,685

* For projects up to December 31, 1938, see 1938 *Annual Report*, U. S. Housing Authority, Table IV. For 1939 projects, USHA press releases, Nos. 242, 253, 275, 298, 317, 335, 374, 390, and 421.

Title II, Sections 207 and 210 of the National Housing Act. Both types of projects are largely of the apartment-type building and are located in approximately the same sized communities. The estimated total average cost of the 138 FHA rental housing projects becoming premium paying by December 31, 1938 was $4,980 per dwelling unit or $1,330 per room.[10] This is comparable to the USHA 1938 cost figure of $5,098 per unit, or $1,244 per room.[11] It must be said in fairness to the USHA that their 1939 approved projects will cost about 15% less than those approved by December 31, 1938, bringing these figures down to approximately $4,300 per unit and $1,050 per room.

The overall cost per dwelling unit of Parkchester, the huge New York City project being built and financed without FHA insurance by the Metropolitan Life Insurance Company, is approximately $4,100.[12] The comparable figure for the three New York City USHA projects approved in 1938 is $5,970.[13]

Other figures on the cost of privately owned and financed residential dwellings are as follows: The average total valuation of house and land of homes financed by the FHA under Title II, Section 203 during 1938 was $5,530. For metropolitan areas the figure is $5,810.[14] The estimated total average value of new homes financed by savings and loan associations during 1938 was $4,270.

In spite of the fact that a cold factual comparison of the costs of USHA-built houses with those privately financed and built for private individuals may not be quite fair to the USHA, it is nevertheless apparent from the foregoing analysis that something is amiss in the USHA scheme of things. It hardly seems logical that middle and upper income groups should be providing slum dwellers with approximately the same priced homes that they are building for themselves.

Using the USHA 1939 total development cost per family unit of $4,575, the cost of housing one family, it would take a capital outlay of some $45,000,000,000 to provide for all urban families that supposedly need

TABLE III. PERCENTAGE OF USHA-AIDED PROJECTS SHOWING ESTIMATED TOTAL COSTS OF DWELLING FACILITIES AND TOTAL COSTS OF HOUSING PER DWELLING UNIT*

(For projects covered by approved loan contracts as of December 31, 1938)

Cost per Dwelling Unit	Dwelling Facilities Cost	Total Cost of New Housing
Under $2,250		
$2,250 and under $2,500	2.16%	
2,500 and under 2,750	2.16	
2,750 and under 3,000	4.32	0.72%
3,000 and under 3,250	6.47	
3,250 and under 3,500	16.54	1.43
3,500 and under 3,750	25.90	2.86
3,750 and under 4,000	24.46	5.00
4,000 and under 4,250	11.51	5.00
4,250 and under 4,500	4.32	12.14
4,500 and under 4,750	2.16	17.86
4,750 and under 5,000		16.43
5,000 and under 5,250		15.00
5,250 and under 5,500		13.57
5,500 and under 5,750		5.71
5,750 and under 6,000		3.57
6,000 and over		0.71
Total	100.00%	100.00%
Weighted Arithmetic Mean	$3,668	$5,098

* Source: see Table II above.

[10] *Fifth Annual Report*, Federal Housing Administration, pp. 121, 122.

[11] See Table III. The average number of rooms per dwelling unit is 4.1.

[12] See *Architectural Forum*, Jan., 1940, p. 3.

[13] Total cost of new housing, from 1938 *Annual Report*, U. S. Housing Authority, Table IV.

[14] *Insured Mortgage Portfolio*, August, 1939, p. 13.

TABLE IV. PERCENTAGE OF USHA-AIDED PROJECTS SHOWING TOTAL DEVELOPMENT COSTS PER DWELLING UNIT*

Total Development Cost per Dwelling Unit	Year Contract Approved	
	Up to December 31, 1938	1939
Under $3,000		4.51%
$3,000 and under $3,250	0.72%	3.01
3,250 and under 3,500		6.02
3,500 and under 3,750	1.44	10.52
3,750 and under 4,000	2.16	9.02
4,000 and under 4,250	2.88	14.29
4,250 and under 4,500	4.32	9.02
4,500 and under 4,750	12.23	9.77
4,750 and under 5,000	15.11	9.77
5,000 and under 5,250	12.23	8.27
5,250 and under 5,500	14.39	4.51
5,500 and under 5,750	7.90	8.27
5,750 and under 6,000	14.39	1.51
6,000 and over	12.23	1.51
Total	100.00%	100.00%
Weighted Arithmetic Mean	$5,534	$4,575

* Source: see Table II above.

housing assistance if we accept the statement that ⅓ of our families need public assistance to obtain adequate shelter.

There are, of course, several unavoidable causes of the high cost of USHA dwellings. The unwarranted high cost of building materials is one fundamental reason. In addition, public housing must be built under strict construction standards and building codes. The fact that the houses must be built to last 60 years makes them somewhat more expensive than private dwellings whose builders do not necessarily aim at 60-year durability. The USHA authorities are honestly attempting to reduce the costs of their houses, and have been moderately successful in doing so, as witness the reduction from 1938 to 1939. Still the fact is inescapable that it appears somewhat extravagant to provide out of public funds money enough to place slum dwellers in *new* homes at anywhere near the capital cost of $4,500 per family. At this rate there will never be enough money to provide better housing for all those that need it.

Opponents of the USHA method of operation have suggested that the rooms be reduced in size, landscaping and ornamentation be eliminated, and the houses or apartments be of cheaper construction. Probably considerable progress could wisely be made in this direction. There can be little social justification for the taxpaying public to bear the cost of anything more than the bare minimum of sanitary and decent housing for slum-dwellers. Probably if public housing projects were built on a lower standard, the housing authorities wouldn't have such a problem on their hands when they have to evict tenants whose incomes have risen above the maximum of five times the rent.

The suggestion has come forward from many quarters that, instead of building new houses for slum-dwellers, existing substandard dwellings be rehabilitated. This appears to be a more satisfactory solution to the problem, as the housing standards of the lowest income groups could thereby be improved satisfactorily and the money available for housing assistance be spread over many more families. The work of Arthur Binns of Philadelphia, about whose work much has been written, gives credence to this proposal. Here, with a total average capital outlay for acquisition and rehabilitation of $1,000 to $1,500 per dwelling unit,[15] slum dwellings were transformed into thoroughly habitable quarters—completely "decent, safe and sanitary" and adequate for any family with a low income.

It appears that the dual objectives of the USHA Act—providing better housing for low income families and stimulating employment in the building trades, which accounts for the necessity of building new homes—may result in the failure of this noble social experiment. One objective may be secondary or the by-product of the other, but linking the objectives together may prove the weakening of the whole program and the failure to accomplish either goal.

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[15] *National Real Estate Journal*, August, 1939, p. 32.

The New Chicago Plan Commission

THE Chicago Plan Commission is now undergoing extensive reorganization which may revive the function of city planning in Chicago to the position it occupied in municipal affairs 30 years ago when the city established one of the nation's first local

planning agencies. The present Commission now being appointed pursuant to a city ordinance adopted on July 12, 1939 is to have the power of preparing and recommending to the City Council "a comprehensive plan for the development of existing property, the rehabilitation of depreciated areas and of public improvements," including also plans for "specific improvements in pursuance of such official plans" or other "improvement plans as may be suggested by officials of the city or by private groups." The Commission is to cooperate with the local housing authority "in the location of housing projects and the elimination of sub-standard housing conditions." It is "to further the making of . . . improvements . . . embraced within the official plan, and generally to promote the realization of the official plan."

The new Commission has a more severe task than its predecessor. The original Chicago Plan, so famous that its models are still available at European exhibits on urbanism, was drawn up by a committee of the Commercial Club of Chicago following the impetus given to the City Beautiful by the first Chicago World's Fair Exposition in 1893. For the purpose of studying further the problems involved in the Chicago Plan with a view to determining "whether it is feasible to adopt any part of said Plan . . . and where to begin," Mayor Busse established the first Plan Commission in 1909. In other words, Chicago had its master plan when it established the 1909 Commission, whereas today Mayor Kelly and the City Council realize that the master plan for the city "Beautiful and Attractive" had been outmoded and that it is not only necessary to draft a new one, but also to set up an informed agency with an experienced staff that will be able to adjust Chicago's physical make-up to the rapidly changing developments of city life.

The new Commission is a step forward in that it is created by city ordinance and therefore has a definite legal basis, whereas the 1909 Commission was established not by ordinance but by "authorizing" the Mayor to appoint a commission as recommended in his "communication" to the Council dated July 6, 1909. The structure of the new Commission is also a more workable one as compared with the earlier Commission which contained 329 members together with the City Council. The new Commission is to consist of 14 appointed members and 12 ex-officio members, including the Mayor and certain council committee chairmen as well as the heads of the Park District, the County Board, and the Sanitary District. A Council resolution also has created a Planning Advisory Board, including not only the members of the City Council but 11 more officials, and 200 citizens appointed by the Mayor.

City planning today is not merely a matter of parks and street layouts as it was when city planning got its start as a recognized municipal function. One of the main tasks of planning in a city like Chicago will be that of cutting through the maze of technical and popular confusion about the structure of the modern city, to analyze the basic population and industrial trends that will tell us which way Chicago seems to be going, to translate these trends into a physical outline for the city livable as well as the city beautiful, to popularize the principal parts of the new Chicago Plan and thereby to win public consent for the execution of the Plan, and to administer the function of investigating and making recommendations to the Mayor, the City Council, and to all city agencies on every single improvement, not merely those on which the Commission is consulted but also projects to which the city is now being committed by its subway, superhighway, and transportation programs.

In carrying out its functions the new Commission will have in its background the earlier traditions and accomplishments of effective city planning in Chicago which dared to go into such new topics originally as union transportation terminals or civic centers. For it should be recalled that, in spite of the more recent leveling off of city planning functions in Chicago, the Chicago Plan Commission had helped realize the Chicago Plan to a degree that has astounded the imagination of many city planners. In 25 years, 98 major projects contained in the Chicago Plan had been constructed, including the widening of Michigan Avenue, the double-decked Wacker Drive, and the magnificent Lake Front Drive. With Chicago's "front yard" in such good shape, the Plan Commission can well afford to attack the deteriorated back yards of the city and the declining areas that are swiftly losing their population and property values to the outlying sections of the city and to the suburbs.

The land use survey, now being conducted, and the 1940 Census will contain data of

great value, depressing or encouraging as they may turn out to be, upon which the Commission's program can proceed. Also available for the service of planning in Chicago is a good deal of engineering experience, management skill, and civic minded leadership. The Plan Commission now contains such names as Ralph Budd, President of the Burlington Railroad; Morton Bodfish, Executive Vice-President of the United States Savings and Loan League; Merle J. Trees, formerly Chairman of the United Charities; Elmer Stevens of the State Street Council; Ray McCarthy, Chairman of the Garfield Park Businessmen's Association; Albert Veeder, well known Chicago attorney, Peter Verschuur, Editor of the *Austinite;* Frank J. Rathje, President of the Chicago City Bank and Trust Company; James E. Bulger, President of the Chicago Motor Club; Albert G. Erdmann, President of the Bell Savings and Loan Association; and Col. A. A. Sprague, who has for years served the city in many capacities and has in the past been Chairman of the Plan Commission. Three more positions remain to be filled and then progress can be made on the important problem of selecting an executive director to build up the staff and program of the Commission. The Advisory Board from which the Plan Commission list is selected contains Chicagoans of ability. Interestingly enough it also contains some of Chicago's traditional names in both city government and city planning. There is, for example, John Wentworth, the namesake of one of Chicago's first mayors, and there is also D. H. Burnham the son of the great Chicago planner who, in its earlier planning days, warned the city in the following words: "Make no little plans; they have no magic to stir men's blood and probably themselves will not be realized. Make big plans; aim high in hope and work, remembering that a noble, logical diagram once recorded will never die, but long after we are gone will be a living thing, asserting itself with ever-growing insistency."

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Federal Inducements for Small-House Construction

RECENT revisions of the regulations set up by the Federal Housing Administration in regard to Title I, Class III loans, together with the RFC Mortgage Company's new policy of purchasing interest-bearing loans made in accordance with these revised rules, will probably stimulate the lending activities of private institutions in the small-house field.

According to the new FHA regulations, Title I, Class III loans are treated more nearly like Title II loans in that: (1) no second mortgage or other junior financing is permitted; and (2) the structure must conform to FHA minimum construction requirements and property standards. In order to assure conformity with construction standards, the FHA is requiring at least three inspections of all houses financed by loans insured under this section of the Act.

The loans are limited to a period of 15 years and 5 calendar months. They bear a maximum interest rate of 4½% per annum plus an annual service charge of ½ of 1% and an annual mortgage insurance premium of ½ of 1% based on the original loan.

Borrowers are required to own an equity in the property financed equal to 5% of its value as appraised by the lending institution. The total amount of each loan is limited to $2,500 or the cost of construction, whichever is less.

Repayments of the loans are made on a monthly basis, the installments covering interest, amortization of the principal, hazard-insurance premiums, estimated taxes, special assessments, and ground rents, if any. In addition, the FHA insurance charge may be included in these installments as well as the service charge.

According to the revised regulations, in case of default the lending institution may foreclose the mortgage, acquire the property and present a claim for insurance under provisions similar in many respects to those in contracts for insurance of small home mortgages under Section 203 of Title II of the Act, or the mortgagee may elect to sell the property and then file claims for its losses over and above the amount realized from the sale. However, a property may not be sold for less than 75% of the unpaid balance without approval of the FHA.

The RFC Mortgage Company has announced a policy of buying interest-bearing Title I, Class III loans if they are used only

to finance new homes constructed after January 1, 1940. However, such loans are purchased only from originating institutions which are financially responsible and qualified to service the loans. Each institution must provide an FHA insurance reserve equal to 10% of the loan and must be located within 100 miles of the mortgaged property.

Loans are purchased at par, a fee of ½ of 1% being charged at the time of purchase and originating institutions may be required to service the loans, retaining the borrower's payment of ½ of 1% plus an additional ½ of 1% as a fee.

The purchase of these loans by the RFC Mortgage Company should increase the volume of funds available for small-house financing in any one community. This policy will tend to modify further the traditionally local character of the mortgage market.

It is probable that these changes in regulations and policies providing more favorable terms of financing will tend to stimulate construction in the small-house field. Future developments alone will determine whether or not this program is a sound one. It may be that financing of this sort involves so many risks that proper allowances for them cannot be made within the framework of the regulations set up. On the other hand, the spreading of such risks over a large number of properties located in many different communities may provide an adequate basis for carrying them.

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New Inquiries for the Census of 1940

FINAL plans have been made for the Sixteenth Decennial Census of the United States, its territories, and possessions. Inquiries in schedule form will cover the vast subject matter coming under the general census headings of population, agriculture, business, manufacturing, mines and quarries, and irrigation and drainage. Enumeration for business and manufactures is already in progress and the canvass for the remaining subjects will commence on the first day of April. Below is a statement of the new inquiries for population, agriculture, and housing. Appropriately, only the briefest mention can be made of some of the probable implications of these data since the returns are not yet available.

Population

The population schedule for the Census of 1940 will be notable for a number of new questions concerning employment status, migration, and education, and for the innovation of the sampling technique to widen the scope of the inquiries. A comprehensive picture of the variations of employment status will be obtained for all persons 14 years old or older by inquiries determining: those employed (actually working or having a job); those unemployed, or new workers, all of whom are seeking work; those engaged in home housework, attending school, unable to work, or retired; the number of hours worked during the week of March 24–30, 1940; the duration of unemployment up to March 30, 1940 in weeks; and the number of full-time weeks worked and the amount of money wages or salary received during the 12 months ending December 31, 1939; the occupation, trade, profession or particular kind of work performed by each worker; the industry or business group in which each worker is employed; and the class of worker, such as employer, own account worker, unpaid family worker, private wage worker, or regular or emergency government wage worker.

The net effects of internal population migration during the preceding quinquennium will be obtained by requesting place of residence for each person as of April 1, 1935 by: state (also territory or foreign country); county; and incorporated place having 2,500 or more inhabitants, or farm or non-farm for residents of rural areas or of places having less than 2,500 inhabitants.

The amount of formal education will be revealed by a question asking for the highest grade of school completed. On the basis of a 5% sample (questions to be asked of each twentieth respondent), the following subjects will be covered: the usual occupation, industry, and worker class as a supplement to information obtained concerning present occupation, in order to determine the availability of and shifts in various kinds of labor; whether the respondent has a Federal Social Security account number and whether wage

deductions have been made for Federal Old Age Insurance during the 12 months ending December 31, 1939; data showing the number of children ever born to women who are or have been married (women married, widowed, or divorced), to make studies of differential fertility; mother tongue or native language obtained by a question asking what language was spoken in the home in earliest childhood; the status of all veterans of foreign wars and their wives, widows, and children; and information concerning the place of birth of the father and the mother of all respondents.

Agriculture

The agricultural schedules for the Census of 1940 likewise have a number of new features. Of major importance is the introduction of nine regional schedules (each to be used in a separate group of states) which are especially designed to fit national variations in cropping practice. Other questions designed to obtain subtotals for the value of various major categories of farm products sold or traded in 1939 will enable a much closer estimate of total farm income and of farm income by principal sources. A supplementary plantation schedule to be used in the cotton belt will make possible a refined distinction between farms as differentiated from plots cultivated by croppers, and the exact status of each cropper and certain other tenants in relation to the plantation owner. New questions designed to serve current agricultural policies will be asked relative to soil improvement crops, summer fallow, crop failure, and succession or interplanted double cropping. Likewise, full information will be obtained concerning irrigated acreage harvested for corn, sorghums, small grains, annual legumes, hay crops, clover and grass seeds, and a number of other miscellaneous crops.

Greater detail will be obtained concerning part-time farming to the end that the number of days will be determined at which each farmer worked for pay or income off his farm, either at work connected with another farm, or, if at non-farm work, by occupation and industry. New inquiries will also be obtained for farm labor by grouping it into classes, by indicating the total number employed on each farm at six months' intervals, and by obtaining the total cash wages paid in 1939.

Other new inquiries likely to prove significant are: the year of the latest model of automobiles, motor trucks, or tractors on the farm; whether the operator does or does not reside on the farm; the number of fur-bearing female animals over three months old and the number of pelts taken in 1939; and the source of electrical power, whether from power line or home plant, and whether or not there is an electrical distribution line within ¼ mile of the farm dwelling.

Housing

In 1940, for the first time, the decennial census will include a separate housing schedule designed to give detailed information for each dwelling unit in the United States, whether occupied or vacant, rural or urban. For each dwelling unit data will be obtained as to the number of rooms, water supply, bath and toilet facilities, and light equipment. For each occupied unit, or household, information will be obtained concerning the principal refrigeration used, the presence or absence of a radio, the character of the heating equipment, and the principal heating and cooking fuels used. In the case of each residential structure it will be determined whether it is for single-, double-, or multiple-family occupancy, whether or not it contains a business unit, for what purpose and in what year it was originally built, the principal exterior material of the structure, and whether it is in need of major repairs. Vacant dwelling units will be identified as to whether they are ordinary dwellings or suitable only for seasonal occupany, whether they are for sale or for rent or held for occupancy of an absent household, and the estimated monthly rental value of each such non-farm dwelling unit. For each non-farm, renter-occupied dwelling unit it will be determined whether or not the monthly rental includes the use of furniture (and, if so, of what value) as well as the average monthly cost of utilities and fuels paid for by the renter in addition to the monthly rental. In the case of the non-farm, owner-occupied dwelling unit an estimate of the market value of the property will be obtained, whether or not there is a mortgage or land contract on the property, and the present amount of the first and second mortgage indebtedness. Finally, for each owner-occupied dwelling unit having a first mortgage or land contract the amount and periods of payment, the interest rates charged, and the

type of corporation holding the mortgage will be determined.[1]

General Considerations

Any prognostications relative to the probable utility of data to be collected under these new inquiries must of necessity be superficial. Not only are no returns available but future requirements cannot be predicted. Notwithstanding these obvious facts one cannot resist the impulse to comment briefly. Regional or city planners, labor-employing manufacturers, retailers, and relief agencies should, among many others, welcome an evaluation of 5-year net population migration. A comprehensive picture of employment status in its many gradations should supply the requisite raw material for a well articulated program of reemployment and for the relief of unemployment. The innovation of the sampling technique in census procedure should not only greatly widen the scope of future inquiries but gain statistical experience with valuable applications in kindred fields. The introduction of regional schedules for the agricultural inquiries should result in detailed data heretofore considered beyond the scope of a census. The agricultural inquiries should throw much light on the national programs of soil conservation, crop insurance, and export subsidy. Rehabilitative agricultural programs designed to alleviate the evils of farm tenancy should be furthered through agricultural data giving: a closer estimate of farm income; the gradations in status from the share cropper to the rent paying tenant to the owner-operator; and the importance of work off the farm. Finally, the detailed inquiries covering the subject of housing have timely significance in connection with the vast building and lending programs of the several federal housing agencies, the activities of numerous city planning and zoning organizations, and the functions of private building and lending groups and individual Realtors.

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[1] It should be noted that the individual returns given for population, housing, and agriculture are cross-indexed to facilitate comparison, checking, and joint use, to the end that all three inquiry categories may be considered essentially as one super schedule.

Land Resources Department

GEORGE S. WEHRWEIN, *Editor*

Rural Zoning in Minnesota

THE recent enactment of a rural zoning enabling act by Minnesota is a landmark in the development of a new land policy for that state. The transition from a forest to an agricultural economy in northern Minnesota, as in the cut-over areas of the other Lake States, has broken down and has not taken place either in the orderly manner or at the rate anticipated prior to 1920. With the breakdown of the process have come many complex problems of low farm income, insolvent local government, and unemployment, familiar to the student of land utilization. During the last decade, a growing public recognition of the fundamental changes that caused the stoppage in this forest-to-farm development has led to the adoption of various legislative measures designed to encourage a more stable development of the region and the restoration of its forest resources.

Prominent among these measures is rural zoning, first adopted in 1933 in Wisconsin as a means of curbing the inefficient expenditure of public funds and of directing settlement to the best agricultural areas of the region.[1] The adjoining Lake States followed the development of zoning, and in 1935 Michigan adopted a rural zoning enabling act.[2] As the culmination of intensive research and discussion by state and federal agencies, the Minnesota legislature in 1939 also authorized the cut-over counties to adopt rural zoning ordinances.[3] In July, 1939 the county attorney for Koochiching County asked the aid of the state attorney general's office in preparing a zoning ordinance, and in answer to this request a proposed ordinance was drafted. Hearings on the ordinance are now in progress, and it is anticipated that the ordinance will be enacted in substantially its present form in the near future. The ordinance is also being used as a model in other northern Minnesota counties where rural zoning is being discussed by county planning committees and other planning groups. Before analyzing the provisions of the act and the proposed ordinance, a brief résumé of the factors leading to passage of the act will be given to illustrate some of the relationships of planning and research to legislative policy.

Background for Minnesota Zoning. The need for rural zoning legislation in Minnesota was first officially recognized by a legislative interim committee, known as the Minnesota Reforestation Commission, which submitted a report to the state legislature in 1928. Governor Olson's Committee on Land Utilization later endorsed the measure as a state policy in 1934. The following year, Nowell and Jesness, in a research study of the northern part of the state,[4] strongly recommended enactment of state enabling legislation and adoption of zoning ordinances by the cut-over counties. In addition, they suggested tentative zoning districts for 14 counties. In 1937, the Resettlement Administration analyzed isolated settlement and tax delinquency in northern Minnesota and pointed out the public finance problems arising from scattered settlement that might be prevented in the future by rural zoning.[5]

The attitude of local people toward zoning was first shown clearly in a planning study of Pine County in 1938.[6] As one phase of the study, investigators of the Bureau of Agricultural Economics obtained specific recommendations from town boards for the zoning of certain districts in the county, which were later submitted to the legislature by county and state officials as evidence of how local

[1] W. A. Rowlands, "County Zoning for Agriculture, Forestry and Recreation in Wisconsin," 9 *Journal of Land & Public Utility Economics* 272–82 (August, 1933).

[2] P. A. Herbert, "Michigan Enacts a Rural Zoning Law," 11 *Ibid.* 309–10 (August, 1935).

[3] Minn. Laws 1939, c. 340.

[4] *A Program for Land Use in Northern Minnesota* (St. Paul: Univ. of Minn. Press, 1935).

[5] *Isolated Settlement and Tax Delinquent Land in Northern Minnesota*, L.U.P. No. 12, prepared by Minn. Land Use Planning Staff, Resettlement Administration, St. Paul, Jan., 1937.

[6] *Land Use Problems and Policies in the Cut-over Regions of Minnesota with Special Reference to Eastern Pine County*, by Roy M. Gilcreast and William F. Musbach, U.S.D.A., B.A.E., St. Paul, Minn., Jan., 1939.

residents would zone if given legal authority. In the summer of 1938, a Legislative Interim Committee on Forestry held five hearings in the northern part of the state, at which time zoning was discussed with local groups. As a result of the hearings, the Committee endorsed zoning and urged the passage of enabling legislation. During the winter of 1938, the county land use planning committee of Koochiching County, on which the entire county board was represented, strongly recommended use of zoning for controlling settlement, submitted a tentative zoning map to the legislature, and pointed out the type of control desired and the districts to be designated if the county board were given authority to zone.

Partly as a result of these research and planning activities and partly as a result of general discussions by state and local officials, popular support for a zoning enabling act was gained, which ultimately led to its passage. Research to determine the problem and the means of attacking it was a fundamental prerequisite, but the translation of plan into legislative policy awaited general public recognition of the need for and the efficacy of the measure, both of which were developed by the hearings of the Interim Committee, the "grass roots" planning work in Pine County, and the county land use planning activities.

The Enabling Act. There are several restrictions on the application of the Minnesota law. Unlike many acts, it is designed primarily for rural areas and does not expressly authorize counties to adopt urban or suburban types of regulations, such as those fixing setback lines, size and height of buildings, and percentage of lot occupied. Furthermore, only counties in which there are state or federal forests or state conservation areas possess the power to zone. This, in effect, confines the application of the act to the northern cut-over region.

The scope of the zoning power is also limited in that a number of land uses are excepted from provisions of the act, including hunting and fishing cabins on privately owned lands, mines, quarries and gravel pits, hydro dams, private dams, flowage areas, transmission lines and substations, and the harvesting of any wild crop. Customarily, these exceptions are made in ordinances rather than in the enabling act. Whether year-round residence in connection with the excepted uses can be regulated is not entirely clear, however. In the draft of an ordinance prepared by the Minnesota attorney general, year-round residence was forbidden in connection with hunting and fishing cabins and the harvesting of wild crops, although it was permitted in conjunction with the other excepted uses.

Similar to many zoning laws, but unlike that of Wisconsin, is a requirement that all zoning regulations must be made in accordance with a comprehensive plan. Since the act expressly allows an ordinance to be adopted for only a portion of a county, it is not clear whether the required comprehensive plan must embrace only that portion of a county to which the ordinance applies, or whether it must include the entire county.

The act provides for the preparation and adoption of an ordinance by a county board, with active participation by town boards. A county board, in conjunction with town boards, is authorized to investigate and determine the need for establishing districts and prescribing regulations and, as a part of the process, to consult with residents and with federal and state agencies. If the investigation indicates that a zoning ordinance is desirable, the county board prepares an ordinance, which must then be approved by the town boards of that portion of the county to which it applies before any further proceedings can be held.[7] If certain of the town boards will not give their approval, the county may eliminate them from the area affected by the ordinance and continue with the proceedings. After approval of the town boards has been obtained, a public hearing

[7] This procedure is adapted from the Wisconsin law, which requires town boards to approve zoning ordinances proposed by a county board, and which contains an additional requirement that an ordinance can be adopted by a county only as to those towns that approve it.

It should be pointed out, however, that in Wisconsin the county board of supervisors consists of the chairman of each town (one of the three members of the town board) together with supervisors elected from each city ward and incorporated village. This means that the town and county are involved in zoning simultaneously because of the "interlocking" nature of these units of government. In Minnesota, on the other hand, the county board consists of five members elected from districts without any relation to towns, which creates a more formal relationship between the two units of government.

is held and the county board may then adopt the proposed ordinance with such changes as it deems advisable. This provision is somewhat ambiguous, however, since the latitude given the county board to make changes is not clear. If a county board could adopt an ordinance radically different from one previously approved by the town boards, the requirement for approval by the latter would become meaningless. It has been suggested that the correct interpretation of the provision would limit the discretion of a county board to alter the draft to include those changes indicated to be desirable by evidence brought forth at the public hearing.

Under the Minnesota act, the county board not only adopts the ordinance, but also acts as a board of adjustment. It is believed that this dual functioning is not authorized by any other rural zoning enabling act, although a similar provision is contained in the Florida soil conservation districts law. It is not clear from the language of the Minnesota law whether a county board can serve as a board of adjustment only during a 60-day period following the effective date of an ordinance, or whether it can act at any time. However, in the draft of a proposed ordinance prepared by the Minnesota attorney general, the view was taken that the power was continuing and could be exercised at any time.

Like most enabling acts, the Minnesota law provides that existing non-conforming uses or occupancies may continue after enactment of an ordinance. If such a use or occupancy is then discontinued for a period of two years, any subsequent use or occupancy must be a conforming one. It also provides that, if the state acquires title to land by tax delinquency foreclosure or otherwise, any further use or occupancy shall conform to the ordinance. The application of this provision is apparently limited to lands acquired by the state after the effective date of an ordinance, and does not expressly relate to those previously acquired. There is thus a possibility that the many thousands of acres of land already acquired by the state through tax delinquency proceedings are not subject to zoning regulations. The act requires a county board, immediately after adoption of an ordinance, to prepare a complete list of all non-conforming uses and occupancies to be filed for record in the office of the register of deeds and the county auditor. Copies are given to town and county assessors for recording the existing non-conforming uses at each assessment thereafter.

The county board is responsible for administration of an ordinance, and is empowered to impose enforcement duties upon any county official or to direct the county attorney to institute appropriate actions to prevent, restrain, correct, or abate any violation or threatened violation. Violations are declared to be misdemeanors and are punishable as such.

The Koochiching County Ordinance. Public attitudes and opinions, however intangible, determine the scope and effectiveness of a zoning ordinance. On the basis of experience gained in classifying lands in connection with the zoning research and planning studies of Minnesota, it can be stated with little qualification that local people regard zoning mainly as an instrument for protecting their pocketbooks by preventing an inefficient expenditure of public funds. Abstract philosophies of "highest and best forms of land utilization" are resolved into concepts of how the building of a $4,000 bridge or the plowing of 10 miles of snow for an isolated settler can be avoided; or what means are available for keeping scattered settlers from starting dangerous fires as part of land clearing operations. To local people, proper land use itself is an indefinite concept. They will admit that certain areas are poorly suited to farming, even though well located, but they usually limit such areas to extremely poor soils since they feel that large parts of the isolated areas are intrinsically productive. Indeed, some opposition has been aroused by use of the terms "nonagricultural" or "forestry" to describe a type of zoning district. At the same time, local residents stoutly defend restrictions on the use of isolated but "productive" lands while those of an equal or superior type remain unused in better settled areas. The designations of the districts—"restricted," "limited," and "unrestricted"—in the proposed ordinance reflect, in themselves, the feeling that agriculture should be "restricted" or "limited" until an anticipated demand for the lands makes it desirable to push out from the present settled communities.

This attitude is also reflected in the manner in which district lines have been drawn under Wisconsin ordinances and under proposed ordinances in Minnesota. With few

exceptions the boundaries of "nonagricultural" or "forestry" districts have been determined largely by the existing settlement pattern. Relatively compact settlements are usually grouped in "agricultural" districts, regardless of the quality of the soil, whereas isolated or sparsely settled areas are usually placed in a "nonagricultural" district, also without regard to soil quality. The primary test accepted by local people is whether or not the use of land for farming will result in an additional expense for school transportation or roads. Thus, although there has been much discussion in terms of prohibiting farming in "forestry" or "nonagricultural" districts, the real objective of local people has been, through zoning, to prevent individuals from demanding the roads, schools, and snow plowing associated with year-round residence in sparsely settled regions, and not to prohibit farming when unaccompanied by high public costs.

In the proposed ordinance for Koochiching County, this objective of local residents is embodied in the regulations effective in the "restricted" districts, which correspond to the "forestry" districts of the Wisconsin ordinances. In the restricted district:

> ". . . no building or structure shall be erected, occupied, or used by any person or persons as an established home, or with intent to establish a home therein . . . unless such home is necessary for use and is used solely in connection with a mine, quarry, gravel pit, hydro dam, private dam, flowage area, transmission line, or substation. Buildings and structures in the process of construction on the effective date of this ordinance may be completed and occupied as homes, free from the foregoing restrictions. The word 'home' as used herein shall not be construed to include any building or structure occupied solely for temporary hunting, fishing, or summer residential purposes, or for the harvesting of wild crops during the legal or customary seasons for such activities."

The effect of this regulation is solely to prohibit year-round residence and not directly to restrict use of land for agricultural purposes. In this respect it differs from the Wisconsin ordinances which forbid both year-round residence and agriculture. The prohibition of year-round residence, in itself, will prevent new settlement which demands roads, schools, and snow plowing, and will thus accomplish the real objective of local groups. Seasonal temporary residence, of course, requires no great outlay of public funds. In addition, the prohibition of year-round residence may be expected to discourage the clearing of additional lands in forested fire-hazard areas, since year-round residence is commonly associated with agriculture in the cut-over counties and "suitcase farming" or absentee farming is not generally practiced.

Another objective of local people is protection of intensive recreational areas. In the northeastern part of Koochiching County, a strip of land along the Rainy River is utilized for summer homes and cabins. The value of this land arises largely from the forests along the river and the natural beauty associated with them. Owners of property in the area desire protection from commercial agriculture with its land-clearing and related farming activities. To meet this objective a "limited" district is established in which:

> ". . . no land in excess of one acre shall be used by any person or family for the production of field or truck crops, livestock, or livestock products. . . . The term 'family' as used herein shall mean only the immediate family, including parents and their children under the age of 18 years living together in the same household; provided, that a guardian or other person having custody of children shall have the same status as parent for the purposes hereof."

By restricting the acreage that can be used for agriculture, it is believed that this potential danger to the recreational area can be removed without prohibiting family gardens. A constitutional question concerning the propriety of drawing a distinction between farming more or less than one acre may be raised, but it is believed that the provision can be upheld on the theory that there is a reasonable classification between the need for permitting family gardens, usually in conjunction with resorts or summer homes, and prohibiting commercial agricultural activities injurious to the recreational nature of the district.

The efficient administration of an ordinance, fundamental to the effectiveness of rural zoning, is dependent upon two factors: (1) the extent to which the objectives of the ordinance are those of local people; and (2) the facility with which violations can be determined. As indicated above, the proposed ordinance embodies the objectives of local people. In order to sharply define violations, the prohibited rather than permitted acts are stated by the ordinance. The effects of the provision are twofold: (1) the regulation is brief and easily understood; and (2) it

embraces a single concept readily capable of interpretation. Instead of determining whether an alleged violation is contrary to a dozen or more permitted uses, it is necessary in "restricted" districts only to ascertain if a person has established or intends to establish a home; and in the "limited" districts, to determine whether a person or family is using more than one acre of land for agricultural purposes. The sharpness of definition obtained by the regulation for "restricted" districts is dependent upon the meaning that courts will give to the word "home." If it is construed to embrace the long established legal concept of "domicil,"[8] which appears to be a logical construction, there should be no difficulty in readily determining whether a certain act is or is not in violation of the ordinance.

In administering the Wisconsin ordinances, difficult and vexing problems have arisen concerning the time of discontinuance of non-conforming agricultural uses under the provision of the law forbidding reestablishment of those that have been discontinued. For example, a non-conforming user may move from his farm, but his land may continue to be used for crops or pasture, either by a lessee or by a trespasser. These uses may be intermittent, such as the occasional cutting of wild hay, or the grazing of livestock when forage is abundant. It is thus difficult to ascertain definitely just when an agricultural use is discontinued. The problem is obviated in the "restricted" districts established by the Minnesota ordinance since prohibition of year-round residence is the sole regulation to be enforced. Instead of investigating intermittent uses of land upon which no one resides, local people and enforcing agencies need concern themselves only with the occupancy of the dwelling. This problem nevertheless remains in "limited" districts under the proposed ordinance, but the relatively small area involved and the small number of non-conforming users reduce its magnitude.

A minor provision of the ordinance is that, unless otherwise noted on the official zoning map, the district lines follow the boundary lines of political subdivisions, center lines of highways or railways, lines established by the United States Government Survey or legal subdivisions thereof, and boundaries of lakes and streams. The purpose of this provision is not to fix the zone lines on these particular boundaries, but rather to act as a guide in the interpretation of the map.[9]

In the establishment of district boundaries, a question of constitutionality is raised by a provision of the Minnesota law that permits the adoption of an ordinance applicable to only part of the county. The law thus authorizes a county board to treat the same type of land differently when it is located in different parts of the county by not including the entire county in districts. Although there are no rural zoning cases on this point, certain court decisions have questioned the validity of urban zoning ordinances that failed to divide the entire municipality into zones.[10] The courts are not agreed on this point, however, and the supreme courts of at least two states (Louisiana and Florida) have expressly held this type of ordinance valid.[11] Whether it is constitutional in Minnesota must be determined by the supreme court of that state.

The most distinctive feature of the proposed ordinance, the separation of occupancy from land-use restrictions, has not appeared in any zoning ordinances heretofore, and experience alone will determine its practical significance. It is believed, however, that it may be applicable in regions outside Minnesota, and research projects are now under way in South Dakota, Oregon, and California, in which an opportunity will be provided for exploring further the possibilities of "occupancy zoning."

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[8] "Domicil" is defined in *Restatement, Conflict of Laws* (1934), §9 as follows: "Domicil is the place with which a person has a settled connection for legal purposes; either because his home is there or because the place is assigned to him by law."

[9] The separation of a "restricted" district from an "unrestricted" district would seldom, if ever, be made on the center line of a road, for example.

[10] *Youngstown v. Kahn Bros.*, 112 Ohio St. 654, 148 N.E. 842 (1925); *City of Aurora v. Burns*, 319 Ill. 84, 149 N.E. 784 (1925); *Miller v. Bd. of Pub. Wks.*, 195 Cal. 477, 234 Pac. 381 (1925).

[11] *State ex rel. Civello v. New Orleans*, 154 La. 271, 97 So. 440 (1923); *State ex rel. Henry v. City of Miami*, 117 Fla. 594, 158 So. 82 (1934).

State Rural Land Use Legislation in 1939†

LAWMAKERS in 44 states met in 1939 for regular annual or biennial sessions. A considerable amount of their legislative output was in one way or another related to rural land use and to land use planning, although the tendency appears to have been in the direction of extension or clarification of previously established trends rather than toward adoption of innovations.

Interstate Compacts. In the field of intergovernmental relations, for example, notable progress was made in the continued development of interstate compacts. New Jersey and New York approved the Delaware River Basin Compact which would divide the basin into four zones and apply minimum standards of sewage and waste treatment within each of the zones.[1] Likewise a water sanitation compact has been negotiated by representatives of eight states in the Ohio River Valley and has been ratified by five.[2] In Connecticut a state commission was created to treat with New York and New Jersey in making plans for prevention of waterway pollution.[3]

West of the Mississippi River, interstate cooperation has been proposed or acted upon with respect to use for irrigation, hydro-electric development, and other purposes, of the waters of the Colorado, Rio Grande, and South Platte Rivers, as well as of the boundary waters between South Dakota and Minnesota.[4]

Federal-State Relations. Further progress was made during the year in formalizing the relationships between the Federal Government and the states in connection with various types of federal aids, acquisition of land for public projects, payments in lieu of taxes, and municipal bankruptcy.

Action was taken by 24 states to meet the requirements of the Pittman-Robertson Federal Aid in Wildlife Restoration Act.[5] This brings to a total of 43, the number of states which have agreed to the conditions set forth in the Act for allocating federal receipts from taxes on firearms, shells, and cartridges to aid in developing wildlife restoration projects.

Great interest was shown in the various proposals before Congress for enactment of some type of federal aid designed to equalize educational opportunities throughout the country without substituting federal supervision for that of the states. Nine states enacted laws accepting anticipated aid or passed resolutions urging that aid be granted.[6]

In Nevada a permanent procedure was established for the acceptance by counties of federal grants-in-aid for public improvements.[7] When the contribution of a county is a very minor one, a resolution of the county commissioners to accept federal aid is sufficient. If the contribution is of a more important character, the commissioners must publish their declaration of intent to accept the aid and voters of the county have 30 days in which to protest.

Several new states were added to the list of those which have consented to the acquisition of land by the Federal Government for use in flood control, soil conservation, power generation, and other public projects.[8] More notable, however, was the tendency to raise the question, in one form or another, of how state and local governments are to be recompensed for the loss of tax-base which results from the increased acquisition of land by federal agencies. Some states were content with memorials to Congress urging that pay-

† For a more detailed summary see "Summary of Outstanding Laws Affecting Rural Land Use Enacted during 1939," *Bulletin* 51, U.S.D.A. (Washington, January, 1940.)

[1] New Jersey, c. 146; New York, c. 600.

[2] The eight states were Illinois, Indiana, Kentucky, New York, Ohio, Pennsylvania, Tennessee, and West Virginia. Of these, Illinois, p. 310; Indiana, c. 35; New York, c. 776; Ohio, S.B. 33; and West Virginia, H.B. 369, ratified the compact.

[3] Connecticut, Special Act No. 65.

[4] The Colorado River Compact is being negotiated by representatives of Arizona, California, and Nevada. Only Arizona, c. 33, has ratified. Colorado, c. 146; New Mexico, c. 33; and Texas, H.B. 152 have adopted the Rio Grande Compact and the Federal Government also gave its consent (Pub. 96, 76th Cong.). Nebraska (c. 53) authorized the appointment of a gubernatorial commission to negotiate with Colorado concerning the waters of the South Platte River; and Minnesota (c. 60) and South Dakota (c. 294) undertook closer supervision of boundary waters.

[5] Public 415, 75th Cong.

[6] Arkansas, Georgia, Minnesota, New Mexico, North Dakota, Tennessee, Utah, Vermont, and Wyoming.

[7] Nevada, c. 148.

[8] Arkansas, Act 327; Maine, Act 248; Massachusetts, c. 284, limited application; and New Hampshire, c. 149, limited application.

ments in lieu of taxes be made,[9] but a greater number passed laws which either declared the property of federal agencies used in "proprietary" enterprises to be taxable to the same extent as privately owned property (as in Alabama and Georgia),[10] or gave counties the right to negotiate directly with the Federal Government.[11]

Still another example of the acceptance by states of the terms of federal legislation was the enactment of laws in nine states authorizing various types of taxing districts to take advantage of the municipal bankruptcy act, which in essence is designed to allow bankrupt units to refund indebtedness, make compositions with creditors, and seek new loans from the Reconstruction Finance Corporation.[12]

Local Government Reorganization. The most unique development in the field of county consolidation for the year came from Tennessee where the legislature not only set up a state committee to deal with the problem in cooperation with the county committee in interested counties,[13] but actually authorized the issuing of $1,000,000 worth of bonds for use in making grants not to exceed $50,000 each, to both absorbed and absorbing counties as an inducement to the carrying out of consolidation plans. The state is to be reimbursed for the grants out of the county's 2¢ share of the gas tax over a period of 20 years.[14]

In North Dakota, constitutional amendments will be submitted to the voters at the next general election which would empower the legislature to provide optional forms of county government,[15] including the county manager form. A novel type of law was also enacted which would permit the disorganization of counties having a population of less than 4,000 inhabitants.[16] A disorganized county would be abolished and powers of all county officials would be transferred to the officials of the adjoining county—the latter to become in no way financially obligated or burdened by reason of the attachment. Two procedures are outlined for the accomplishment of this end, the first being initiated by petition followed by an election and the second by petition and judicial determination by the district court.

Nebraska also has a constitutional amendment ready for submission to the voters in November, 1940 which would permit counties to choose between optional forms of county government.[17] Colorado legislators, however, took a more conservative stand on county reorganization and went on record as deploring the fact that smaller counties were being forced to surrender their identity and accept, against their will, annexation to adjoining counties.[18]

There was a continued trend toward the encouragement of functional cooperation between local governmental units. Fulton County, Georgia, for example, was authorized to make contracts with the City of Atlanta for the performance of administrative, protective, and other governmental functions and services.[19] In Nevada, any county containing a city fire district will be allowed to make agreements with the city fire department for assistance in protecting property in rural areas.[20] In Tennessee, cooperation between counties and municipalities and cooperation between adjoining counties are authorized when agreed to by their respective legislative bodies.[21]

Several significant measures were enacted in the field of township, school, and highway reorganization. In Arkansas the old form of local road district was replaced by a county unit system.[22] County courts were also given power to change school district boundary lines upon the written consent of boards of directors and of a majority of the electors in the districts and territory affected.[23] In Idaho, all highways are declared to constitute a state-wide highway system and, although the local governmental units continue to con-

[9] Florida, H.M. No. 3 and North Carolina, c. 236.

[10] Alabama, Gov.'s No. 65; Georgia, No. 203; these acts contained the proviso that state taxing power was to be used only within the limits of constitutional authority.

[11] Alabama, Gov.'s No. 65; Arkansas, Act No. 361; Oklahoma, c. 66; Montana, c.'s 58 and 59; New York, c. 823.

[12] Arkansas, Act No. 69; California, c. 1017; Colorado, c.'s 124 and 164; Idaho, c. 110; Michigan, Act No. 72; Montana, c. 114; North Carolina, c. 203; Oregon, c. 109; and South Carolina, c. 40.

[13] Tennessee, c.'s 224 and 225.

[14] Tennessee, c. 226.

[15] North Dakota, c. 112.

[16] North Dakota, c. 122.

[17] Nebraska, c. 25.

[18] Colorado, S.J.R. No. 11.

[19] Georgia, Act No. 276.

[20] Nevada, c. 57.

[21] Tennessee, c.'s 222 and 223.

[22] Arkansas, Act No. 379.

[23] Arkansas, Act No. 387.

struct and maintain roads within their respective limits, they now do so as agents of the state.[24] In Indiana, additional limitations are placed upon the powers of boards of county commissioners to divide counties into townships or to change the number, names, and boundaries of existing townships.[25] County committees are created in Oregon in all those counties which have not elected to come under a previously enacted county school law, for the purpose of investigating the effectiveness of existing school district boundaries and acting with the State Board of Education in preparing a comprehensive school district plan to be completed by September 1, 1940.[26] Pennsylvania and Utah likewise took action to bring about better school organization, the former by establishing a uniform procedure of school district mergers[27] and the latter by creating a gubernatorial committee to make an exhaustive study of the school system.[28] In South Dakota, highway boards are abolished in those unorganized counties where less than 12½%, by area, of all real property remains on the assessment lists or where the assessed valuation is not more than $500,000.[29]

Planning and Zoning. Several states enacted rural zoning laws and New Mexico established a state planning board but planning boards were abolished in North Dakota, South Dakota, and Oregon,[30] so that developments in this field cannot all be described as positive. Colorado and Minnesota adopted rural zoning enabling acts effective in all counties of the former and in all counties in the latter having a state or federal forest or a state conservation area. The Colorado law[31] authorizes boards of county commissioners to plan and zone unincorporated territory as well as to cooperate with governing bodies of municipalities and of other counties in carrying out a regional planning and zoning program. Preparation of a master plan is authorized on a county or regional basis and may include a wide range of subjects. The scope of zoning ordinances is more restricted and it is not altogether certain that it includes regulation of agricultural land use.

The Minnesota enabling act[32] is more closely tied into township organization. The board of county commissioners, in conjunction with the township boards, acts as a zoning commission and ordinances establishing districts and prescribing regulations must be approved by township boards in the areas affected. The zoning power cannot be used to regulate use of land for hunting, fishing, cabins, mines, quarries, gravel pits, hydrodams, private dams, flowage areas, transmission lines and substations, or for harvesting any field crop.

Tennessee provided for the creation of community planning commissions to aid in the accomplishment of a coordinated, adjusted, efficient, and economic development of unincorporated communities. These communities are to be set aside by action of the state planning commission and may not exceed 10 square miles in area although they must have at least 500 inhabitants. The action must be initiated by means of a petition signed by local freeholders.[33]

Seven Georgia counties were affected by special acts authorizing varying degrees of building and land use regulation in unincorporated areas.[34] Two special zoning acts were passed in Kansas which apply to unincorporated areas in a very limited number of counties, but here again the power to regulate land use is narrowly confined.[35] Voters in Anne Arundel County, Maryland, will be called upon in November, 1940 to act upon a new zoning enabling law,[36] and the County Court of St. Louis County, Missouri, has been authorized to do suburban type zoning in the unincorporated areas of that county.[37]

Forestry. The New Mexico legislature undertook to regulate the lumbering industry in the state by establishing certain minimum requirements to be observed by loggers for

[24] Idaho, c. 16.

[25] Indiana, c. 150.

[26] Oregon, c. 468.

[27] Pennsylvania, Act No. 275.

[28] Utah, c. 82.

[29] South Dakota, c. 111.

[30] New Mexico, c. 158; North Dakota, c. 203; South Dakota, c. 210; Oregon, c. 551.

[31] Colorado, c. 92. See George S. Wehrwein, "The Colorado Planning and Zoning Enabling Act," 15 *Journal of Land & Public Utility Economics* 483–5 (Nov., 1939).

[32] Minnesota, c. 340; see William F. Musbach and Melville C. Williams, "Rural Zoning in Minnesota," *supra* pp. 105–9.

[33] Tennessee, c. 158; see Howard K. Menhinick, "County Zoning by Indirection," 15 *Journal of Land & Public Utility Economics* 482–3 (Nov., 1939).

[34] These were Bibb, Camden, Clayton, Fulton, McIntosh, Paulding and Richmond counties.

[35] Kansas, c.'s 164 and 165.

[36] Maryland, c. 633.

[37] Missouri, p. 662.

the prevention and suppression of fire and the protection of young trees during operations.[38] The most interesting feature of the law is the requirement that a certain number of seed trees be left standing for each acre of cut-over land.

The State of Washington enacted legislation which would permit state officials to enter into cooperative agreements with the Federal Government and with private timber owners for the purpose of coordinating sustained yield forest management practices,[39] while Alabama, Missouri, New York, Tennessee, Texas, Vermont and West Virginia undertook to clarify and extend the scope of criminal statutes dealing with the setting of fires which constitute a menace to forest resources.[40] In Florida and South Carolina, districts have been created in specific counties designed especially to deal with forest fire problems.[41] In Nebraska, Oregon, and Washington, so-called rural fire protection districts are provided for but these have no relationship to forested areas.[42]

Montana made a virtually complete revision of all state forest fire protection laws including a reorganization of the state board of forestry.[43] Minnesota has appointed an interim forestry legislative commission to study and investigate forest fire protection, windbreaks, forest taxation, state aids for long-time forestry programs, and other matters pertinent to the development of an adequate state-wide policy.[44]

Grazing. The outstanding grazing district legislation for the year was enacted in Montana when the state grazing laws were revised and the Montana Grass Conservation Commission was substituted for the state grazing commission.[45] Increased powers were also given to grazing associations over lands lying within district boundaries. No one may now graze livestock within a district without a permit from the association unless it be grazed upon land owned or controlled by him and restrains his stock from trespassing on lands controlled by the association. This provision allows the association to regulate the grazing of unfenced lands and those that have been abandoned by their owners. Both Nevada and New Mexico undertook to clarify the procedure for distributing the money paid into the state treasury by the Federal Government as a share of the returns from grazing leases in Taylor grazing districts.[46] Alabama enacted a local option stock law which allows the voters in each county or district to say whether or not cattle are to be allowed free range.[47]

Soil Conservation Districts. Ten new state soil conservation enabling acts were adopted during the year and eight old laws were amended.[48] As in the past, the new acts conform rather closely to the Standard Act[49] drafted by the Department of Agriculture, the essential features of which are too well known to require further exposition here.[50]

Variations from the Standard Act which might be mentioned include the provision in the amended Florida act[51] abolishing the state committee and transferring its powers and duties to the State Board of Control. In the new Texas act,[52] voting members of the state committee are selected by a system of conventions and elected delegates beginning with meetings of landowners in the precincts of each county.

Nearly all the new acts and several of the amendments require that only owners of land sign the petition for organization or vote in the various referenda. Likewise, nearly all require that more than a majority of those voting be favorable to organization or to the adoption of particular land use regulations. The Oregon act[53] is particularly note-

[38] New Mexico, c. 144.

[39] Washington, c. 130.

[40] Alabama, Gov.'s No. 492; Missouri, p. 347; New York, c. 96; Tennessee, c. 213; Texas, S.B. 102; Vermont, Temp. No. 54; W. Va., c. 64.

[41] Florida, c.'s 19, 274; S. Carolina, c.'s 102, 144 and 310.

[42] Nebraska, c. 38; Oregon, c. 347; Washington, c. 34.

[43] Montana, c. 128.

[44] Minnesota, c. 418.

[45] Montana, c. 208.

[46] Nevada, c. 67; New Mexico, c. 125.

[47] Alabama, Gov.'s No. 368.

[48] New laws were enacted by Alabama, Idaho, Iowa, Montana, Oregon, Tennessee, Texas, Vermont, Washington, and West Virginia. Former acts were amended in California, Colorado, Florida, Illinois, New Mexico, North Dakota, Pennsylvania, and Wisconsin. See Melville C. Williams and H. L. Price, "Law of the Land: 1939," *Land Policy Review* (July-August, 1939).

[49] *A Standard Soil Conservation Districts Law* (Washington, 1936).

[50] See H. A. Hockley and Herman Walker, Jr., "1937 State Legislation for Control of Soil Erosion," 14 *Journal of Land & Public Utility Economics* 210–7 (May, 1938).

[51] Florida, c. 19,473.

[52] Texas, S.B. 20.

[53] Oregon, c. 555.

worthy in this connection because it requires that ¾ of the majority of votes cast representing ⅔ of the land favor the adoption of land use regulations before they can be effective.

Variations in the methods of selecting district supervisors are found in several of the new acts as well as in the amendments to old ones. In Alabama, for example, the supervisors are all appointed by the state committee.[54] Florida now requires that all five supervisors be elected and that any five of the original petitioners perform temporarily the functions formerly performed by the two members appointed by the state committee. In Iowa three supervisors are regularly elected but the two state committee appointees continue in office only until that is accomplished.[55] Montana districts elect five supervisors except that two state committee temporary appointees serve at the outset for terms of one and two years, respectively.[56] In the amended Wisconsin act, the members of the "Special Committee on Agriculture," previously created to assist county agricultural agents, are made ex officio district supervisors.[57] The amendment also provides that new districts be organized, not by action of the state committee pursuant to petition, hearing, and referendum, but simply by county boards of supervisors—their boundaries to be coterminus with those of the county.

The Idaho and Iowa acts[58] have omitted the provision for adopting and enforcing land use regulations which is found in the Standard Act and the Vermont Act[59] contains an incomplete provision for the consideration of regulations but authority for the district supervisors to enact and enforce them has apparently been omitted.

New Mexico has a unique amendment[60] which requires the state committee to determine what part of each district is range land and what part farm land. Two of the three elected supervisors are named by owners of land in that zone ("range land" or "farm land") containing the larger proportion of the total number of landowners, and the other by the landowners of the other zone. Land use regulations must be separately submitted for each zone, and landowners vote only on those regulations applicable to their zone.

Land Tenure. Many states extended the effective dates of their mortgage moratorium laws[61] and in Iowa the spirit of the original law was embodied into permanent form so as to allow owners of lands foreclosed for defaults necessitated by natural catastrophies or by economic depression duly proclaimed by the Governor, to apply for a continuance of the foreclosure proceedings.[62]

California authorized the formation of voluntary farmer associations to procure the refinancing of their indebtedness by financial institutions on the State Farm Debt Adjustment Commission's approved list. Although a loan advanced by the lending institution constitutes a direct obligation of the individual farmer to whom it is made, each member of the association assumes liability for any deficiency of his brother members.[63]

Efforts to improve the legal relationships between landlord and tenant were given something of a setback in Oklahoma when the 1937 "Farm Landlord and Tenant Relationships Act," designed to facilitate progress through educational programs and the working out of an arbitration system, was repealed.[64] Further relaxation, however, of restrictions on the sale of public lands for farms on long-term sale contracts, as prescribed in newly enacted laws, tend in some measure to show that the subject of land tenure is not being overlooked by Oklahoma legislators.[65]

Public Lands. The accelerated rate at which county and state governments have been getting title to tax reverted and foreclosed lands has caused no little increase in the interest shown by legislators in the problems of public land management. Several significant advances have been made in the clarification of policy both on a state and county basis.

In Arkansas, state-owned lands may now be classified by the Land Use Committee of the State Planning Board into three groups:

[54] Alabama, Gov.'s No. 147.
[55] Iowa, c. 92.
[56] Montana, c. 72.
[57] Wisconsin, c. 323.
[58] Idaho, c. 200; Iowa, c. 92.
[59] Vermont, Temp. No. 202.
[60] New Mexico, c. 163.

[61] Arizona, California, Michigan, Minnesota, Montana, New York, North Dakota, Ohio, and Wisconsin.
[62] Iowa, c. 245.
[63] California, c. 929.
[64] Oklahoma, c. 53, Art 1.
[65] Oklahoma, c. 28, Arts. 2 and 3.

(1) lands to be retained in public ownership, (2) lands suitable for agricultural settlement, and (3) lands to be returned to private ownership. Lands classified as suitable for agricultural settlement include those that can be developed into new agricultural communities by clearing and drainage operations. This class is apparently intended to be transferred to the Federal Government for development. Lands classified as suitable for return to private ownership may be returned by sale or donation as determined by the classifying body. Donation of tracts either greater or less than a family-sized farm is not to be allowed.[66]

South Dakota enacted county land management legislation which permits county boards to classify land according to the method of leasing and sale to be followed.[67] Class I land is that which may be sold or leased as in the past; Class II land is that which seems most likely to remain in county ownership for a relatively long period of time pending tax adjustments or conservation development. Another feature of the law is the provision for land exchanges. Similar land exchange laws were enacted during the year in other states, attesting to the wide recognition of the value of this type of measure in blocking out land management units.[68]

Indiana and Ohio made progressive changes in their methods of handling tax delinquent lands. Neither the state nor its subdivisions could acquire title to chronically delinquent lands under previous laws. Now those chronically delinquent lands which it appears will best serve that purpose may be designated as "conservation lands" and may be acquired through tax foreclosure procedure. When title has been confirmed in the state, they may be sold, exchanged, leased, or otherwise disposed of in such a manner as will best accomplish their proper utilization and conservation.[69]

Minnesota also adopted a classification measure to be applied to all tax reverted lands that become the absolute property of the state, when they are situated within any conservation or reforestation area. Lands classified as non-agricultural are reserved by the state to be dedicated to conservation purposes, whereas agricultural lands may be disposed of at public auction in parcels of not more than 160 acres. Pending sale, they may be leased.[70]

Another interesting development during the legislative year in connection with land management was the number of laws passed to authorize longer terms of lease for grazing lands in the western states. The usual five-year period has now been increased to 10 in Montana and North Dakota; and a constitutional amendment was proposed in Arizona which would accomplish the same purpose.[71]

Taxation. Legislative indulgences, so common throughout the country during the past decade, have been continued in many states in the hope of encouraging the payment of delinquent taxes and improvement district assessments. For the most part they involve the abatement of interest and penalties, installment payments, or extension of the redemption period.[72]

One of the novel developments in the taxation field was the establishment of an "Agricultural Land Credit Fund" in Iowa. In order to relieve inequitable and disproportionate burdens of school taxes levied in independent school districts, $500,000 of state money is to be earmarked annually for the fund and owners of agricultural lands within such districts are privileged to petition the county assessor for a credit on the general school taxes. The amount of the credit is to be equal to the amount by which the general school fund levy exceeds 15 mills.[73]

Another noteworthy trend is manifested in the number of states which have undertaken comprehensive revisions of their revenue and taxation codes. California, Illinois, North Carolina, Oklahoma, Oregon, and Wisconsin may be mentioned among states which have completed either whole or partial revisions.

In Colorado, all parcels of real estate (outside incorporated areas) for which a county

[66] Arkansas, Act No. 331.

[67] South Dakota, c. 25. See Raymond Penn and Harry A. Steele, "Land Management in South Dakota," *Land Policy Review*, p. 33 (Nov. and Dec., 1939).

[68] Minnesota, Montana, North Dakota, Oregon, and South Dakota.

[69] Indiana, c. 153; Ohio, H.B. 478.

[70] Minnesota, c. 302.

[71] Montana, c. 65; North Dakota, c.'s 218 and 237; Arizona, H.C.R. 3.

[72] Alabama, California, Idaho, Illinois, Iowa, Kansas, Michigan, Minnesota, Nebraska, New Mexico, Ohio, Oklahoma, Pennsylvania, South Dakota, Tennessee, Washington, and Wisconsin.

[73] Iowa, c. 109.

holds tax sale certificates in any one year may now be included in a single request for a tax deed. Likewise, individuals owning certificates of sale may include as many as 25 tracts in a single tax deed application, even though each tract was sold separately at the tax sale. In both cases, a single notice of application is sufficient.[74]

In Missouri, lands twice offered at regular delinquent tax sales, and twice failing to attract a bid high enough to clear up the delinquency, are to be sold to the highest bidder at the next annual sale. The redemption period formerly allowed after this third sale has been eliminated by the present enactment and the purchaser gets a tax deed at once.[75]

New York made important changes in its delinquent tax enforcement procedure. One of the new features is the provision allowing taxing districts to include all delinquent tax liens of at least four years standing in a single *in rem* foreclosure action. Costs are thereby considerably reduced and the individual taxpayer's rights are not necessarily jeopardized since he may always file an answer to the collective action with reference to his own particular tract.[76]

Water Utilization. Interstate compacts for preventing stream pollution or for determining water rights have already been mentioned. A quantity of intrastate water utilization measures were also written into law during the year. They range in detail from minor procedural changes in the registration of water rights to the adoption of state-wide programs for water conservation.

In Montana, a law was enacted which would permit the complete adjudication of water rights along streams and their tributaries pursuant to an action brought by the state engineer at the direction of the State Water Conservation Board.[77] Nevada provided a method for the registration of underground water rights in artesian well basins.[78] North Dakota adopted a water conservation law which creates a State Water Conservation Commission with power to supervise and regulate sale of water rights, distribution of water, and construction and operation of water works.[79]

The creation of new taxing districts to be known as water conservancy districts is authorized in South Dakota. This authorization is supplementary to powers already granted by other statutes to organize irrigation districts and districts for the storage, purchase, or distribution of water for municipal purposes.[80] A general enabling act for the development of flood control districts in and around certain classes of cities was passed in Indiana, and several special flood control districts were established in California.[81]

New or amended procedures for the dissolution of drainage districts in South Dakota, Utah, and Washington also remedied an undesirable lack of flexibility in existing statutes in those states.[82]

Summary. In selecting the laws to which reference has been made in the foregoing paragraphs, no thought was given to geographical relationships. It is only fair, therefore, to point out that every one of the 44 states whose legislatures met in 1939 took some action which could be interpreted as being beneficial to the solution of rural land use problems in a broad sense. No widespread innovations are discernible, such as the soil conservation district or rural zoning acts of earlier years, but there is ample evidence that the trend of legislative policy has changed from one of indifferent exploitation to that of long-range planning and conservation of agricultural resources.

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[74] Colorado, c.'s 144 and 145.
[75] Missouri, p. 850.
[76] New York, c. 692.
[77] Montana, c. 185.
[78] Nevada, c. 178.
[79] North Dakota, c. 256.
[80] South Dakota, c. 291.
[81] Indiana, c. 23; California, c.'s 73, 420 and 656.
[82] South Dakota, c. 290; Utah, c. 35; Washington, c. 149.

Public Utilities Department

E. W. Morehouse, *Editor*

Exemption of Small Rural Telephone Companies from the Wage and Hour Act

"Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 13(a) of the Act approved June 25, 1938 (52 Stat. 1069), entitled the 'Fair Labor Standards Act of 1938,' be, and the same is hereby, amended by adding a new subsection 11 as follows: 'or (11) any switchboard operator employed in a public telephone exchange which has less than five hundred stations.' Approved, August 9, 1939."[1]

Passage of the brief act quoted in full above exempted thousands of small rural telephone exchanges from the wage and hour provisions of the Fair Labor Standards Act, and thereby saved thousands of small independent companies from financial failure, saved their employees from loss of their jobs, and prevented drastic curtailment of telephone service in small communities and rural areas. A brief review of the problems those companies would have faced if they had been required to comply with the minimum wage and maximum hour provisions of the Fair Labor Standards Act may help indicate the desirability of that exemption.

Wage and Hour Requirements in Relation to Size and Operation of Small Telephone Companies

There are substantially more than 7,000 small independent rural telephone companies in the United States. The approximate size of those independent companies may be illustrated by the following data for companies operating in Wisconsin:

Annual Gross Operating Revenues	Number of Independent Telephone Companies in Wisconsin	Approximate Number of Exchanges under 500 Stations	Approximate Number of Exchanges over 500 Stations
Over $100,000 (Class A)	4	130	15
$50,000– 100,000 (Class B)	6	10	5
10,000– 50,000 (Class C)	60	80	30
3,000– 10,000 (Class D)	120	110	10
Under 3,000 (Class E and smaller)	570	570	0

Most of the exchanges operated by Class A, Class B, and Class C companies have less than 500 stations each, and practically all exchanges operated by Class D companies have less than 500 stations each. Practically none of the Class E and roadway companies have any exchanges with over 100 stations, and most of these companies have less than 50 total stations. Most of the smaller-than-Class D companies were organized by farmers for their own service, and even Class C and D companies may be truly characterized as neighborhood businesses.

Even though the exchanges with less than 500 stations usually provide 24-hour service, the operator is generally busy only a few hours during the day, may have to answer only a few calls at night, and has enough time available for other activities. Accordingly, many of the smallest exchanges are operated on a contract basis in private homes in conjunction with a small store, or with the normal household work.

The wages and hours determined by the normal employment agreement between employer and employee, and by state regulations before the Fair Labor Standards Act was passed, recognized these operating conditions and the fact that the number of hours which operators actually worked on calls was far less than the number of hours spent on the premises. Thus, in Wisconsin, for example, the maximum hours were determined in accordance with the Industrial Commission's graduated scale of permissible hours of work, as contrasted with *hours on premises*.[2]

[1] Public No. 344, 76th Cong., 1st Sess., c. 605, S. 1234.

[2] The Wisconsin Industrial Commission's scale of *hours of work* is as follows:

Number of Telephones	Hours Counted from 10 P.M. to 6 A.M.	Total Hours Counted per Day	Maximum Hours' Work Permitted	
			Per Day	Per Week
250 and under	1	17	10	60
251 to 499	2	18	10	60
500 to 749	3	19	9½	56
750 to 999	4	20	9½	56
1000 to 1249	5	21	9	56
1250 to 1499	6	22	9	56
1500 to 1999	7	23	9	56
2000 and over	8	24 {day / night}	9 / 8	50 / 48

Similarly, minimum wages were determined in accordance with a graduated scale of *hours of pay*, contrasted with *hours on premises*. Operators received the standard rate of 22½¢ per hour for each *hour of pay*. Pay for operation of exchanges in private homes could, as an alternative, be computed at 45¢ per month per phone.

The Fair Labor Standards Act, however, provides that, after the wage and hour provisions became effective, employees were to be paid at the rate of not less than 25¢ an hour in the first year, 30¢ an hour in the second to seventh years, and 40¢ an hour thereafter, and employees were not to be required to work more than 44 hours per week in the first year, 42 hours per week in the second to seventh years, and 40 hours per week thereafter unless they were paid time and one-half for overtime. In the absence of any other indication, it appears that hours on the premises were to be used in determining minimum wages and maximum hours. The great difference between the former Wisconsin and the new federal requirements may be illustrated by the fact that the payroll for operators in exchanges of only 200 stations providing 24-hour service would be $19.60 per week, or approximately $1,000 per year under the Wisconsin scale, and $50.40 per week or approximately $2,600 per year under the federal requirements beginning in the second year.

Financial Inability of Companies to Meet Requirements of the Act

It would have been literally impossible for the companies to meet this additional cost. Even before passage of the Fair Labor Standards Act, small rural companies were in financial difficulties. Many were operating at a loss, and few were able to make adequate provisions for depreciation and replacement.

Conservative estimates made by the Wisconsin Public Service Commission indicate that most of the Class C and Class D companies would have had to double their payrolls to comply with the new federal requirements. Those additional payroll costs imposed by the Act would have wiped out the operating income of practically all Class C and D companies, and would have resulted in substantial operating losses (before interest or return). Even the largest independent telephone company in the state (because its predominant business is operation of many small exchanges providing service in small communities and rural areas) would have been unable to meet its bond interest and preferred stock requirements if forced to meet the increased costs imposed by the federal Act. Clearly, if Class D and larger companies could not meet the standards of the Act, it would have been a sheer impossibility for the 570 smaller-than-Class D companies (whose gross operating revenues in many cases were less than ½ the new minimum annual payroll requirement) to meet the federal requirements. The Wisconsin Telephone Company, however, because it operates in practically all large cities of the state and carries on relatively little business in rural areas, would be able to meet the federal requirements at the very small additional cost of approximately 1% of the company's net operating income. The wages of this company were relatively equal to, or higher than, those prescribed in the Act, but since the company's hours in some cases were somewhat longer than the maximum, it would be obliged to increase payments for overtime.

Alternatives Considered by the Telephone Companies

To meet these difficulties, many smaller companies considered the following three principal alternatives:

1. Rate Increases. Rates in many cases would have had to be doubled to cover the higher payroll costs. However, experience during the past decade indicates that rural companies cannot increase their rates without danger of a substantial decrease in the number of subscribers who can afford to pay for service. That loss of subscribers might, in many cases, be so extensive that the company would not be able to operate economically and would have to abandon service entirely. In this respect the small telephone companies differ from other utilities which can pass increased wage costs on to the consumer without a substantial loss of customers.

2. Automatic Switching. Most small companies do not have, and in many cases would not be able to obtain, the capital necessary to purchase automatic switchboard and dial equipment. In those few cases where companies could change to dial equipment, that change would result in discharge of their operators—a result not in accord with the declared policy of the Act to eliminate detri-

mental labor conditions "without substantially curtailing employment or earning power."

3. Curtailment of Service. Elimination of night and holiday service or severance of connections with the Bell System for long distance service, in order to avoid any interstate calls and thereby confine their operations to local service which would be exempt from the Act, obviously would be an unpopular backward step. This destruction of the advantages of telephone communication which rural users need would cause a loss of subscribers which might force the companies to abandon operations.

If the companies followed any of these alternatives there would be a great danger that people in rural areas and small communities would be unable to obtain satisfactory service at rates which they could afford to pay. Under these circumstances the state commissions, including the Wisconsin Commission, were faced with numerous inquiries and applications for relief from the burdens of this Act. To carry out their responsibility for maintenance of adequate service and reasonable rates, the commissions considered various possibilities for obtaining relief for the small rural telephone companies.

Proposed Methods for Obtaining Relief for Small Rural Telephone Companies

At first it was thought that, because these companies were predominantly local intrastate businesses, they might be excluded from the coverage of the Act in accordance with the terms of Section 13(a). That section excludes from the wage and hour requirements of the Act "(2), any employee engaged in any retailing or servicing establishment, the greater part of whose selling or servicing is in intrastate commerce." However, in the General Counsel's Interpretative Bulletin No. 6, the companies' claim to this exclusion was in effect denied, subject, however, to the possibility of further consideration.

The Administrator was likewise urged to issue an order or regulation which would modify the requirements to make them consistent with the nature and operations of these small companies. The position of the Administrator, however, as indicated by the General Counsel's Interpretative Bulletins Nos. 1 and 5, was that "The statute does not confer upon the Administrator any general power to issue rulings including industries within the coverage of the Act, or excluding them." Although this did not eliminate the possibility of a subsequent interpretation of hours of work which might provide some relief, no definite action was taken along that line. Under these circumstances, it became apparent that, if small rural telephone companies were to obtain relief at all, such relief would have to come through a Congressional amendment exempting them from the provisions of the Act.

Congressional Action over Proposed Amendment

Numerous bills were introduced in Congress to provide an exemption for the small rural telephone exchanges with less than 1,000 stations. Action centered, however, on the bill introduced in the House on March 29, 1939 by Chairman Mary T. Norton of the House Labor Committee. That bill, supported by Wage and Hour Administrator Elmer F. Andrews, contained limited amendments designed to clarify the Act, to permit more flexible administrative action, and to prevent actual hardships in cases where the Act was unworkable. Incorporated in that bill was a provision, exempting from the wage and hour provisions, telephone exchanges with less than 350 stations.

The exemption for telephone exchanges was, however, soon caught in the Congressional fight over other amendments to the Wage and Hour Law. Opponents of the law, composed in part of the so-called farm bloc of the large agricultural employers and processors together with political opponents of the administration, would not let any bill pass unless it contained the major amendments they desired which would withdraw large groups of employees from the coverage of the Act. Administration leaders wanted to pass the Norton bill but would not permit any wholesale amendments to pass which would have emasculated the Act.

Until the final days of the session, when each side had blocked the other in the fight over the major amendments, it was impossible for the telephone exemption to pass. However, both the administration and the opposition recognized the non-controversial fact that exemption for small rural telephone companies was essential if they were to continue in existence. Accordingly, the separate bill S. 1234 providing an exemption for tele-

phone exchanges with less than 500 stations was passed by the Senate on August 1, 1939, and by the House on August 3, 1939, and was approved by the President and became effective on August 9, 1939.

The very fact that this exemption passed by unanimous consent, and is the first and only amendment to the Fair Labor Standards Act of 1938, supports further the conclusion that the exemption of small telephone exchanges was indeed highly desirable.

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Public Utility Financing in the Fourth Quarter of 1939 and a Summary of the Year, 1939

Fourth Quarter Financing

PUBLIC utility security offerings totaled $364 millions in the fourth quarter of 1939. This compares with $505 millions offered in the fourth quarter of 1938 and with $389 millions offered in the previous or third quarter of 1939.[1]

Total offerings in the present quarter are only slightly below the third quarter of 1939, indicating a resumption of utility financing after the sharp drop in war-disturbed September and October.

Long-term bonds, excluding serial issues, totaled $338 millions, or 93% of total offerings, in the fourth quarter of 1939. Serial obligations offered amounted to $22 millions (or 6%) and preferred stocks to $4 millions (or 1%) of total public utility offerings.

Private sales of long-term debt issues amounted to $183 millions or 54% of the total long-term bonds offered in the fourth quarter. The trend in private placing of long-term debt issues for the period 1936–39, inclusive, is analyzed in Part II of this study. The security flotations in the fourth quarter continue to be mostly for refunding purposes, with new capital requirements continuing to be relatively negligible.

Long-Term Debt Financing. The 24 issues in this classification are shown in Tables I and II, for publicly and privately offered issues, respectively. Table I includes 7 issues totaling $155,400,000 which were offered publicly in the fourth quarter of 1939. The weighted average offering yield (3.63%) is the highest of any quarter in 1939. Underwriters' commissions and incidental expenses are about average. The weighted average cost to company shown in Table I is about the same as the average for the second and third quarters.

Seventeen issues totaling $183,126,000

[1] The summary for the third quarter (see the November, 1939 issue of the *Journal* at p. 489) shows a total of $456 millions. This total has been revised to exclude the New York Power & Light Company's issue ($67 millions) which was delayed by the war and finally completed in the fourth quarter.

TABLE I. SUMMARY AND ANALYSIS OF PUBLIC UTILITY LONG-TERM DEBT ISSUES OFFERED PUBLICLY, FOURTH QUARTER, 1939

Company and Issue (A)	Coupon Rate (B)	Principal Amount (C)	Maturity Date (D)	Month of Offering (E)	Offering Price (F)	Offering Yield (G)	Underwriters' Commissions (H)	Proceeds to Company (I)	Estimated Incidental Expenses (J)	Net Proceeds (K)	Cost to Company (L)
Pub. Serv. Co. of Colorado	%				%	%	%	%	%	%	%
First mortgage	3½	$40,000,000	1964	November	102.00	3.38	2.00	100.00	.86†	99.14	3.55
Sinking fund debentures	4	12,500,000	1949	November	102.00	3.75	1.50	100.50	.86†	99.64	4.04
Central States Electric Co.											
First mortgage	4	2,250,000	1964	December	102.00	3.87	2.75	99.25	1.02‡	98.23	4.10
Northern Ind. Pub. Serv. Co.											
First mortgage	3¼	45,000,000	1969	December	100.00	3.75	2.00	98.00	.58	97.42	3.90
Pennsylvania Wtr. & Pr. Co.											
Ref. and collateral trust	3¼	10,900,000	1964	December	104.00	3.02	2.33*	101.67	.82	100.85	3.20
Pub. Serv. Co. of Indiana											
First mortgage	4	38,000,000	1969	December	102.00	3.89	2.00	100.00	.62‡	99.38	4.04
Southwestern Lt. & Pr. Co.											
First mortgage, A	3¼	6,750,000	1969	December	102.00	3.64	2.00	100.00	.61	99.39	3.79
Weighted Average or Totals		$155,400,000			101.56	3.63	1.99	99.57	.71	98.86	3.80

* Includes an additional fee of ¼ of 1% to Aldred and Co.
† Partially estimated. Expenses prorated.
‡ Pro-rata share of expenses.

were sold privately during the quarter. Fourteen of these issues are analyzed in Table II; the three remaining ones are listed in a footnote to that table. The weighted average offering yield is 3.47%. Incidental expenses, including finder's fees,[2] average .66% for those issues for which data were obtainable, which compares favorably with the figure of .71% of par value shown for publicly offered issues.

Other Utility Financing. Issues with serial maturities offered in the fourth quarter are listed as follows:

$10,000,000	Public Service of Indiana 3 7/8s of 1940–49 at $101.50 average.
6,000,000	Northern Indiana Public Service 2 7/8s due in 20 semi-annual installments at $100.
4,800,000	Dresser Power Corp. 4s of 1942–58 at $100.
750,000	Central States Electric Co. 4 1/2s of 1945–52 at $100.
$21,550,000	

[2] Information on finder's fees and other expenses for current privately sold long-term issues is now available and will be shown in subsequent articles as additional information.

Fourth quarter offerings of preferred stock were limited to one issue—$4,000,000 Wisconsin Michigan Power Co. 4½% cumulative, par $100, priced at $100 to yield 4.50%. The Securities and Exchange Commission in its Release No. 1742 (October 5, 1939) announced that the Philadelphia Electric Co. would issue $10,000,000 of 2¾% serial promissory notes, due 1940 to 1949, and 50,000 shares of no par $4.25 dividend preferred stock to be sold privately. No record of the completion of this sale has been found and therefore the foregoing securities were excluded from fourth quarter totals.

II. Summary of the Year 1939

In spite of a rather slow start during the first quarter of the year and an almost complete cessation of activity during September as a result of uncertainty created by the war in Europe, public utility security flotations

TABLE II. SUMMARY AND ANALYSIS OF PUBLIC UTILITY LONG-TERM DEBT ISSUES OFFERED PRIVATELY, FOURTH QUARTER, 1939*

Company and Issue (A)	Coupon Rate (B)	Principal Amount (C)	Maturity Date (D)	Month of Offering (E)	Offering Price (F)	Offering Yield (G)	Incidental Expenses: Finder's Fees (H)	Incidental Expenses: Other Expenses (I)	Incidental Expenses: Total (J)	Net Proceeds (K)	Cost to Company (L)
New York Telephone Co.	%				%	%	%	%	%	%	%
Refunding mortgage	3⅜	$75,000,000	1964	October	99.50	3.41	†	†	†	†	†
New York Power & Lt. Corp.											
First mortgage	3¾	66,582,000	1964	October	104.14	3.50	none	.55	.55	103.59	3.55
Northwestern Electric Co.											
First mortgage	4	6,700,000	1964	October	100.00	4.00	.52	.44	.96	99.04	4.06
Debentures‡	4½	2,800,000	1959	October	100.00	4.50	none	.44	.44	99.56	4.53
Caribou Water, Lt. & Pr. Co.											
First mortgage, A	3½	275,000	1964	October	105.00	3.21	1.00	2.00	3.00	102.00	3.38
Citizens Gas Co.											
First mortgage	4½	225,000	1959	November	100.00	4.50	†	†	†	†	†
Associated Telephone Co.											
First mortgage	3½	10,300,000	1969	November	105.75	3.20	†	†	†	†	†
Long Island Water Corp.											
First mortgage	4	2,144,000	1964	November	104.00	3.78	†	†	†	†	†
Pennsylvania Tel. Corp.											
First mortgage	3¼	4,800,000	1969	November	101.25	3.19	†	†	†	†	†
Central Main Power Co.											
First and gen. mortgage, K	4	1,250,000	1964	November	100.00	4.00	.50	1.57	2.07	97.93	4.13
California Public Serv. Co.											
First mortgage	4¼	500,000	1964	December	100.00	4.25	1.00	1.50	2.50	97.50	4.42
Potomac Electric Power Co.											
First mortgage	3¼	5,000,000	1974	December	105.31	2.99	.30	.28	.58	104.73	3.01
New Mexico Gas Co.											
First mortgage, B	5	250,000	1954	December	100.50	4.95	2.00	1.50	3.50	97.00	5.29
Virginia Public Serv. Gen. Co.											
First mortgage, S.F.	4	1,400,000	1959	December	100.00	4.00	1.11	1.04	2.15	97.85	4.16
Total or Weighted Average		$177,226,000			101.92	3.47	—	—	—	—	—
Total or Weighted Average (excluding issues for which incidental expenses were not available)		$ 84,757,000			103.59	3.57	.10	.56	.66	102.93	3.62

* Excluding 3 issues totaling $5,900,000 for which no data on prices or expenses were available. These issues are:
(1) Arizona Edison Co. 1st mtge. 4's of 1959, $2,700,000.
(2) Continental Telephone Co. Collateral Trust 4's of 1959, $2,700,000.
(3) California Water Service Co. 1st Mtge. 4's of 1961, $500,000.
† Data not available.
‡ Sold to holding company (American Power and Light Co.).

during 1939 totaled $1,337 millions, as compared with $1,230 millions in 1938, $803 millions in 1937, and $2,123 millions in 1936. The 1939 total is 9% greater than that for 1938 and almost double the total for 1937, but was substantially lower than that for 1936.

Table III submits data showing the composition of public utility financing by quarters from 1936 to date. As is explained in a footnote to this table, no common stocks or short-term obligations, excepting serial maturities, are included. Virtually all common stock issues during the period shown were taken by holding companies and it is difficult to make a complete record of such transactions. Public offerings of common stock totaled less than $1,000,000 for the entire period. Complete data on short-term issues are also difficult to obtain, although it is known that public offerings of short-term notes and securities were minor in amount.

Long-term bonds make up a high percentage of total utility flotations throughout the period. Issues of this classification are subdivided between those offered publicly and those sold privately. It will be noted that the total volume of issues sold privately has become increasingly important in the total. If this trend continues, it may have far-reaching effects in limiting the selection of securities available to the public. The majority of issues sold privately are usually purchased solely for the institution making the purchase and are not ordinarily subject to resale.

TABLE III. VOLUME OF PUBLIC UTILITY FINANCING, BY QUARTERS, 1936 TO 1939, INCLUSIVE‡

Year and Quarter	Long-Term Bonds*				Serial Offerings†		Preferred Stock†		Total in Millions
	Public Offerings		Private Offerings						
	Millions	Per Cent of Total	Millions	Per Cent of Total	Millions	Per Cent of Total	Millions	Per Cent of Total	
1936		%		%		%		%	
1st	$364	86	$ 56	13	$ 4	1	—	—	$424
2nd	510	83	28	4	54	9	$ 24	4	616
3rd	238	76	71	23	1	—	4	1	314
4th	719	93	31	4	—	—	19	3	769
Total	$1,831	86	$186	9	$ 59	3	$ 47	2	$2,123
1937									
1st	$274	72	$ 19	5	—	—	$ 85	23	$378
2nd	185	92	10	5	$ 4	2	1	1	200
3rd	66	73	3	3	18	20	4	4	91
4th	87	80	11	10	10	9	1	1	109
Total	$612	79	$ 43	5	$ 32	4	$ 91	12	$778
1938									
1st	$106	68	$ 49	31	—	—	$ 1	1	$156
2nd	179	75	55	23	$ 2	1	2	1	238
3rd	240	73	81	25	5	2	1	—	327
4th	350	69	81	16	55	11	19	4	505
Total	$875	71	$266	22	$ 62	5	$ 23	2	$1,226
1939									
1st	$ 96	64	$ 18	12	—	—	$ 36	24	$150
2nd	203	46	181	42	$ 3	1	48	11	434
3rd	247	64	63	16	32	8	47	12	389
4th	155	43	183	50	22	6	4	1	364
Total	$699	53	$445	33	$ 57	4	$136	10	$1,337

* Exclusive of serial offerings.
† Includes issues sold privately as well as publicly.
‡ Exclusive of short-term obligations (other than serial issues) and common stock issues. No attempt has been made to summarize short-term borrowings because of the impossibility of obtaining complete data. Public offerings of common stock have been negligible throughout the period.

Private sales of long-term bonds were particularly large in the fourth quarter of 1939, when they accounted for more than ½ of the total long-term offerings. This is traceable to the fact that private sales accounted for virtually all offerings in October and November. Apparently it took more time for public offerings to recover from the effect of the outbreak of hostilities in Europe than it did in the case of private sales.

Table III does not supply a direct measure of the comparative importance of public and private offerings of long-term bonds because of the inclusion in the table of other types of security offerings. Such a measure is shown below:

	Per Cent of Public Utility Long-Term Bond Flotations Sold Privately*
1936	9%
1937	7
1938	23
1939	39

* Excludes serial issues.

Offerings of preferred stock recorded a large increase in 1939 as compared with other recent years. It is noted that the trend toward this type of security was interrupted in the fourth quarter.

Table IV summarizes yield and cost data on long-term bonds offered publicly by quarters from 1936 to date. This table should not be interpreted as indicative of the trend in interest rates during the period. Not only do the figures on offering yields, for example, reflect changes in interest rates, but they also reflect changes in the quality of issues offered. The slight upward movement in the weighted average of offering yields which is shown in 1939 as compared with 1938 probably is traceable to a change in quality of issues offered.

Offerings of bonds of a speculative nature on a comparatively high-yield basis have been relatively rare in recent years and all but disappeared in 1939. Very few public utility bonds were offered at a price to yield more than 4%. Underwriters' commissions averaged close to the customary 2% and were slightly higher on the average than in 1938. Incidental expenses were also slightly higher in 1939 but the increase was not

TABLE IV. SUMMARY OF YIELD AND COST DATA OF PUBLIC UTILITY LONG-TERM DEBT ISSUES OFFERED PUBLICLY (EXCLUSIVE OF SERIAL MATURITIES), 1936 TO 1939, INCLUSIVE

Year and Quarter	Number of Issues	Offering Yields		Underwriters' Commissions		Estimated Incidental Expenses		Cost to Company	
		Range	Weighted Average	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average
1936		% %	%	% %	%	% %	%	% %	%
1st	17	3.25–5.48	3.64	1.00–6.00	2.25	0.42–2.27	0.58	3.40–6.09	3.82
2nd	26	3.05–5.00	3.78	0.97–4.00	2.26	0.35–2.15	0.91	3.13–5.75	4.00
3rd	18	3.15–4.77	3.46	0.75–3.50	2.18	0.51–2.38	0.84	3.28–5.23	3.63
4th	32	3.00–4.87	3.37	0.74–3.25	2.06	0.23–1.68	0.54	3.12–5.38	3.51
1937									
1st	12	3.19–5.11	3.48	2.00–5.00	2.02	0.48–4.16	0.58	3.34–5.81	3.61
2nd	8	3.25–4.69	3.61	2.00–3.25	2.06	0.29–1.90	0.64	3.41–5.17	3.78
3rd	6	3.37–5.28	3.69	1.99–4.00	2.02	0.51–3.69	0.84	3.53–6.25	3.86
4th	5	3.50–4.56	3.82	2.00–3.50	2.12	0.62–1.62	0.88	3.99–5.23	4.05
1938									
1st	4	3.39–4.44	3.86	2.00–2.50	2.27	0.54–1.02	0.61	3.55–4.76	4.05
2nd	7	2.92–6.18	3.40	1.03–8.00	1.73	0.36–6.57	0.57	3.11–7.65	3.58
3rd	12	3.00–5.00	3.43	0.50–3.50	1.80	0.50–2.18	0.74	3.13–5.38	3.58
4th	12	3.01–6.20	3.44	0.96–5.00	1.98	0.32–3.33	0.58	3.15–6.91	3.59
1939									
1st	6	3.15–4.00	3.58	1.75–4.00	2.09	0.61–1.48	0.81	3.32–4.22	3.81
2nd	14	2.75–5.75	3.56	1.00–4.10	2.01	0.39–6.91	0.70	2.89–6.36	3.73
3rd	11	2.69–4.20	3.44	1.50–3.00	2.03	0.39–3.42	0.66	2.77–4.44	3.60
4th	8	3.02–3.89	3.63	1.50–2.75	1.99	0.58–1.02	0.71	3.20–4.10	3.80

sufficiently large to be of marked significance. The weighted average cost of capital to the company followed much the same trend as the offering yield and in no case during 1939 was the "spread" between the two more than .23%. This, of course, does not refer to individual issues but to the weighted averages.

The following summary shows that 78% of the larger long-term debt issues had a term of 25 years or more. The majority of issues mature in either 25 or 30 years. The figures indicate that institutional buyers purchasing privately offered issues apparently preferred 25-year maturities:

Term in Years	Large Long-Term Debt Issues Offered during 1939*			
	Number of Public Offerings	Number of Private Offerings	Combined Public and Private	
			Number	Per Cent
Less than 20	5	2	7	12%
20	3	3	6	10
25	11	11	22	37
30	14	7	21	35
More than 30	2	2	4	6
Total	35	25	60	100%

* Excluding serial issues and issues of less than $1,000,000 par value.

High-Lights of the Year's Financing

North American Company Issues. This company offered a total of $105 millions in debentures and preferred stock. The debentures were of somewhat shorter than average duration, being 10, 15, and 20 years. Offering yields on the debentures were fairly low, varying from 3.29% on the 10-year maturity to 3.91% on the 20-year maturity. The preferred stock sold at a price to yield 5.53%. The operation was noteworthy in that holding companies have participated to only a slight extent in recent years in the movement to refinance.

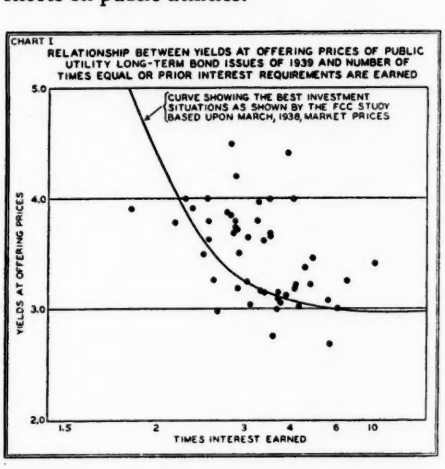
Commonwealth Edison Company's issue of 3¼s of 1979 totaled $114,500,000 and is one of the largest issues ever sold privately. It was sold at a price to yield 3.16%.

Southern Bell Telephone and Telegraph Company's issue of 3s of 1979 sold at a price to yield only 2.69% and the total cost to the company was only 2.77%.

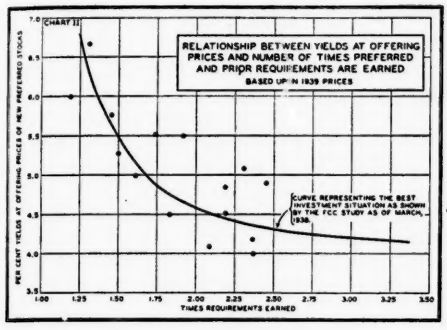
Consolidated Gas Electric Light and Power Company of Baltimore sold an issue of 4¼% preferred stock, amounting to $22,306,300, at $112.50 to yield only 4%. The same company marketed $7,000,000 in 3% bonds at a price to yield 2.75%.

Relationship between Times Requirements Earned and Yields at Offering Prices

Charts I and II have been prepared in order to show the relationship between the relative quality (as measured by times requirements earned) of new capital issues and the offering yield. These charts help to fill a gap in the quarterly security compilations. It is rather difficult to obtain ratings of new securities when first offered and this lack of information affects the quarter-to-quarter comparisons of weighted average yields and net costs to the utilities. Data on times interest earned for long-term bonds on Chart I and times preferred and prior requirements earned on Chart II were obtained from SEC releases, prospectuses, and Moody's advance sheets on public utilities.



The curves plotted on each chart are not fitted curves, although the curve on Chart II appears at first glance to be a curve fitted to the plotted points. The curves represent the best investment situation as found in the Federal Communications Commission's study, "The Problem of the Rate of Return in Public Utility Regulation," pages 114 and 132. The curves roughly define the lowest points in the field (as of March, 1938, based on market prices of selected utility bonds) and were accepted as evidence of the scale of investors' valuations of debt and preferred capital issues under the most favorable con-



ditions, with respect to factors other than earnings coverage.

The curve on Chart I indicates the character of the demand for debt issues.[3] The yield drops rapidly as requirements approach 3 times interest earned. Beyond 3 times interest earned the drop in yield becomes relatively insignificant and the earnings ratio no longer is the controlling factor. The same comments hold for Chart II but the point of decreasing rate of decline in yield is not so well defined, being somewhere between 1.75 and 2 times requirements earned.

The plotted points on Charts I and II represent all new bond and preferred stock issues offered in 1939 for which earnings could be obtained. An optimum curve based on 1939 data would fall somewhat below and roughly parallel to the plotted curve. The difference approximates the shift downward in the costs of bond and preferred stock capital since March, 1938.

Because of the variety of conditions affecting the individual issues, it is hazardous further to interpret the indications of these charts. If the sample were classified and additional curves were fitted to the data and if similar comparisons were made for other periods, clearer indications of the significance of "times requirements earned" might be found.

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[3] The horizontal scale on Chart I is hyperbolic, and in effect shows the same thing as if the proportion of income required to meet interest were plotted on an arithmetic scale, with 100% at the beginning or left side of the scale.

Book Review Department

Urban Land

Aronovici, Carol. HOUSING THE MASSES. *New York: John Wiley & Sons, Inc., 1939. pp. xv, 291. $3.50.*

In some ways this is the most significant addition to the literature of housing which has appeared in many a day. It is in no sense a simple introductory little manual or ABC vade mecum of the subject nor on the other hand is it an exhaustive encyclopedia. It represents primarily an insistence upon and a contribution to the understanding of sociological and economic fundamentals in the whole problem of housing, but with special reference, as the title indicates, to housing for the great masses of our population below the affluent income level.

The author is no novice in this field. He has been studying and working in it for the past 30 years. He brings to it a close familiarity with European housing movements and European social and economic thought. Dr. Aronovici has produced a book which challenges the thinker. He offers no easy solution and does not for a moment permit us to believe that housing the masses is an easy problem. He bears down at every point upon its complexity and its difficulty. The book is refreshing because of its essential realism. It is not pessimistic but on the whole conservatively melioristic. And it is frankly not a flash-in-the-pan production, taking advantage of a fad of the moment, nor does it seek entirely local or immediate solutions to housing problems. It conceives of housing as a long-range problem.

The author assumes that the sanitary regulations and legal minimum standards of safety and finance can without much difficulty be established by law; the engineers and lawyers could take care of such matters. But the sociologist speaks when he insists that "What is more difficult is to create conditions which would make housing embodying these standards financially practicable and accessible to all families as owners or renters." In the attempt to solve the very large number of social, economic, and legal problems involved in this view it seems necessary to work out a "restatement of the housing problem as a sociopolitical philosophy in which public action and private enterprise would be brought into effective relationship in the interest of building enterprise and particularly housing." For this reason from the very start he insists that the housing problem is vastly more than mere slum clearance. He lays bare the real issues by his bold statement that "If we could forget the slums for a decade and proceed to develop housing where there is no decay and no mis-management of investment or unwarranted speculation, we would open the road to decent housing, which the insistence upon slum clearing only delays."

The author lays great stress upon such points as the suitability of land for housing purposes, the flight of population from the center to the periphery of our cities, the tendency of timid zoning efforts to destroy stability and raise false hopes, land "sweating," the relation between elasticity of land exploitation and service expansion, the killing frost effects of the heavy burden of special assessments, the heavy cost of buildings, the effect of radical changes in the size and composition of families, the increasing number of non-farm rural families, wages, legal restrictions, municipal land ownership, transportation, decentralization, and a score of other important topics. He makes it very clear that, even if land were given away in certain cities, the present cost of buildings would make rentals in new dwellings prohibitive for a large proportion of our people. He maintains rightly that the whole program of housing depends upon careful consideration of population trends. He condemns severely the sentimentality which frequently overstimulates home ownership and declares flatly that under present conditions "the agencies which aspire to encourage and promote home ownership are a menace to the economic structure of the country."

The author's whole attitude may be summarized in the statement that "housing is a public necessity like shipping, roads, and a water-supply and waste-disposal system. The question is not who is to pay for it, but how it is to be provided. The responsibility rests with the governing bodies, and the cost should be met by the people as they meet all other necessities." It is evident that

to establish in practice such a principle will require a considerable period of education not only in housing, but in sociology, engineering, architecture, and economics. For this reason Dr. Aronovici includes not only interesting sections on the subject of housing education and housing service, but also a valuable analytical appendix on housing literature. The conclusion is inescapable that housing is not a synonym for slum clearance but involves the whole social texture of individual and community thinking. Housing reform then would require that "a whole new set of fundamental social, economic, legal, and technological principles must be woven into a philosophy of living which will find final expression in a program of housing the masses under community conditions intended to conserve not alone health, but every effort and aspiration which has individual and social value."

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Land Resources

Marquis, Ralph W. ECONOMICS OF PRIVATE FORESTRY. *New York: McGraw-Hill Book Co., Inc., 1939. pp. viii, 219. $3.*

Impressed with the significance of present-day change in the forest industry of the nation—a change greater than the public in general realizes—the author has provided a timely publication covering the problems of an industry in transition. A roving frontier industry, having almost completed its exploitation of a natural resource, is now giving thought to the need of growing recurring forest crops if it would continue to harvest. The timber industry's apparently belated concern as to perpetuation of our commercial forests is but a repetition of the history of forestry in other countries. "The practice of forestry by private initiative has never thrived as long as there was an abundance of virgin timber to be obtained almost without cost for the manufacture of forest products."

This conclusion is reached after reviewing the evolution of forestry in this country, beginning with the doctrine of inexhaustibility, passing through the era of an approaching timber famine when forests were to be hoarded for the future and the use of wood substitutes was advocated as a conservation measure, to the modern concept of sustained yield forestry with research and trade promotion to enable wood to hold its markets.

The author's fear, as expressed in the preface, that foresters may find much to criticize, is not well founded. The book reveals a sound understanding of forestry principles and logging methods, and their economic significance. Strangely enough, it was in the field of taxation that this forester found what he regarded as the only serious omission. Except for comment that the tax on undistributed corporate income tended to discourage industrial forestry, there is no mention of federal taxation. In view of the author's recognition that stock in forest and timber industries is often held within a single family, the effect of the inheritance tax to force liquidations of timber holdings, perhaps destroying a small sustained yield operation, might well be pointed out. Also, federal income tax regulations require the reporting of forestry cost paid out of earnings as capital investment, whereas the Wisconsin income tax law permits reporting such expenditures as operating costs.

The effect of these two provisions might well be discussed, especially when those practicing selective logging or leaving protected seed trees can lose their forestry costs in logging costs, but the operator who engages in large-scale planting has no such escape.

In general, the text is clear, logical, and impartial. It recognizes the need for public forests but reserves a major role for private enterprise. The public benefits of soil and moisture conservation and flood reduction resulting from private forests are pointed out along with the fact that the public is responsible for most of the fires destructive to private forests. Perhaps the public can obtain the benefits of forests cheaper by encouraging private forestry than by buying them, paying for operation, and losing the tax income. Forest protection, equitable taxation, and long-term, low-rate credit are among the inducements which are advocated, leaving regulation to bring into line those who fail to adopt better practices.

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Wisconsin Department of Conservation